THE ONE BILLION DOLLAR QUESTION:
How Can Tanzania Stop Losing So Much Tax Revenue
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June 2012
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The report has been commissioned by the Interfaith Standing Committee on Economic Justice and the Integrity of Creation. The committee is comprised of religious leaders from TEC, BAKWATA and CCT.

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Our sincere thanks to Norwegian Church Aid (NCA) and staff for not only the financial support availed but also the continued partnership in implementing our development agenda.

The Most Rev. Paul R. Ruzoka

Chairperson ISC

Disclaimer: The views contained in this report do not necessarily reflect the views of the interfaith standing committee or the religious leaders. A significant degree of due diligence has been exercised in preparing this report but the Interfaith Committee can not be held liable for any factual errors or misrepresentation of data or otherwise which may be contained in the report.

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For more information please contact Christian Council of Tanzania

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Foreword

The Interfaith Standing Committee on Economic Justice and the Integrity of Creation (ISCJIC) is a faith-based committee comprising of religious leaders from Christian Council of Tanzania (CCT), Tanzania Episcopal Conference (TEC), and The National Muslim Council of Tanzania (BAKWATA). The committee was formed in 2008 to facilitate religious leaders to effectively advocate for social and economic justice. This resolve emanates from the fact that advocating for the rights of the marginalized, the poor, and the voiceless is one of the cornerstones of the constituting faith.

The One Billion Dollar Question is a product of the study commissioned by the interfaith committee to establish the magnitude of tax revenue losses in Tanzania and to recommend measures to minimize such losses. The report estimates that Tanzania, one of the poorest countries in the world, is losing around 1 billion dollar in tax revenue annually mostly through tax evasion, capital flight and tax incentives.

Although the government is taking some steps to improve tax revenue collections, Tanzania needs a fresh, more radical approach to raising sufficient tax revenues, from businesses operating in the country. It is hoped that this report, which makes several recommendations to the government, will help in this process. Developing an effective tax system in Tanzania is vital not only since it can generate increased revenues for the government to invest in social and economic development in order to eradicate poverty, but also, effective tax systems can help countries escape dependence on foreign aid or finite natural resource, thus helping to diversify a country’s economic base. An effective tax system is critical in promoting democracy – by reinforcing the legitimacy of the government and promoting the accountability of the government to its citizens. How well government money is spent is a sign of how deep a democracy and functioning state really is. And how fairly government revenues are raised is a sign of how equitable a society’s development is.

This report is a continuation of another study commissioned by the ISC. In 2007/8 the Committee commissioned a study entitled Golden Opportunity which carried the theme of 'How Tanzania is failing to benefit from gold mining'. The Golden Opportunity report showed that Tanzania was failing to benefit significantly from gold mining.

We pray that this report be an eye opener for Tanzanians to realise how much of our financial wealth is lost as a result of tax policies. This is the money that could have gone towards building that one dispensary, a school, roads, enable access to water or any other development activities that would have benefited Tanzania.

We as religious leaders believe that the economic situation in Tanzania will improve if the government takes seriously the recommendations given in this report.

God bless Tanzania.

Christian Council of Tanzania

Tanzania Episcopal Conference

The National Muslim Council of Tanzania
THE ONE BILLION DOLLAR QUESTION: How Can Tanzania Stop Losing So Much Tax Revenue
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Summary

This report analyses Tanzania’s tax policies and how much revenue the country is losing from tax evasion, capital flight and tax incentives. It shows that, every year, a vast amount of potential tax revenue that could be used to reduce poverty is failing to end up in the government treasury; much is simply leaving the country.

Increasing the revenues available to the government is especially critical during the current global financial crisis when countries are even more vulnerable to shocks. The issue of fair taxes is also vital in light of future income from Tanzania’s recently-discovered oil and gas. Although the government is taking some steps to improve tax collections, Tanzania needs a more radical approach to raising sufficient tax revenues. It is hoped that this report, which makes several recommendations to the government, will help in this process.

Tanzania collected TShs 4.5 trillion ($2.8 billion) in taxes in 2009/10. Of these, around 30 per cent came each from Value Added Tax (VAT) and income tax while excise duties accounted for around 18 per cent and import duties for around 9 per cent. Tax collections amount to only around 15 per cent of GDP in Tanzania, lower than 19 per cent in neighbouring Kenya and around 30 per cent in developed countries.

Tax incentives

Tanzania provides an array of tax incentives and exemptions, especially to mining companies and firms operating in the Export Processing Zones (EPZs). Many of these exemptions represent an unnecessary loss of revenue. Exemptions given to corporations have deprived Tanzania of an average of TShs 458.6 billion ($288 million) a year in the three years 2008/09 – 2010/11.

The government claims that the tax incentives offered in the EPZs are necessary to attract foreign investment. But the key question is whether the extent of these exemptions is justified in terms of the foreign investment that results. Our analysis is that Tanzania has lost more revenues from tax exemptions given to corporations in the last three years than it has received in all foreign investment since the EPZs were established in 2002.

Mining companies are paying around $100 million a year in all taxes which amounts to less than 7 per cent of the value of mineral exports – their tax payments are low mainly because of the tax incentives they receive. Moreover, around 65 per cent of mining taxes are paid by employees of the companies, in the form of Pay As You Earn (PAYE), not by the companies themselves. The new mining act, passed in 2010, brings some important changes to the mining sector but in effect applies only to new projects since existing gold mines remain governed by the generous fiscal terms and tax stabilisation clauses outlined in individual mineral development agreements.

Trade mis-pricing and capital flight

Further revenue losses are resulting from capital flight, which can be either legal or illegal, but means money leaving the country. This report is concerned with the illegal variety – also called illicit financial flows - which entails the disguised expatriation of money abroad, usually to developed countries or tax havens. This can involve transactions arising from criminal activities, corruption or tax evasion by transnational corporations. The latter can take various forms, especially a phenomenon known as ‘trade mis-pricing’, which involves a multinational company deciding the allocation of profits between its subsidiaries by inflating or deflating import or export prices for goods ‘traded’ between those subsidiaries, in order to reduce its tax liability.

Figures suggests that illicit capital flows from Tanzania range from $94 – 660 million a year and that illicit flows from trade mis-pricing alone amount to $109 – 127 million a year. These already large figures are likely to be gross under-estimates due to the lack of accurate data. One expert working on this issue in Tanzania
estimates that such flows could be close to $1 billion a year, with trade mis-pricing alone responsible for around $500 million. In terms of tax revenue losses, we estimate that the illicit flows could cost the Tanzanian government up to $300 million a year, of which revenue losses from trade mis-pricing amount to up to $150 million a year. Our research has also found that many large companies operating in Tanzania use tax havens in their corporate structures, increasing the possibility both of perfectly legal (but still often ethically questionable) tax avoidance and also of illicit capital flight.

**Tax evasion and revenue loss**

A 2008 study for the World Bank found that business managers in Tanzania estimated that firms report only 69 per cent of their sales for tax purposes. We calculate that if Tanzania’s current tax revenues from corporations amount to only 69 per cent of the correct figure, then the country is losing a further TShs 240 billion ($151 million) a year.

Trade across Tanzania’s borders is also believed to be under-reported, and involves smuggling and reducing payments of taxes such as import duties. A survey by the East African Business Council found $602 million worth of unrecorded or undervalued cross-border trade transactions at Namanga, on the Tanzania-Kenya border, in 2007. Illegal activities that involve tax evasion are believed to occur in various sectors. In forestry, for example, a 2007 report authorised by the Ministry of Natural Resources and Tourism on the logging boom in southern Tanzania found that revenue losses amounted to $58 million a year due to under-collection of natural forest product royalties in the districts.

In 2010, the Tanzania Minerals Audit Agency (TMAA) audited 12 mining companies and raised a number of ‘queries’ concerning some companies’ financial claims. It alleged that some unspecified companies had over-declared their capital allowances and operating expenditures, among other areas – a process which would have reduced their tax liability. Such over-claims came to a total of $705.8 million, according to the TMAA. Many of these queries received responses from the mining companies, which reviewed and discussed them among their management, but the TMAA noted that there remained ‘unresolved queries’ amounting to $251 million. We estimate that the original alleged over-claims of $705 million could have resulted in a tax liability of around $176 million. Since 2010 was the first year in which the TMAA had conducted such audits, it is possible that, based on the TMAA allegations, similar alleged over-claims could have been made by some companies in previous years.

The failure to collect taxes from the informal sector, which accounts for 40-60 per cent of GDP, also produces large revenue losses. A recent report by the Tanzania Revenue Authority estimates that around 40 per cent of firms in the informal sector do not pay taxes. Most actors in the informal sector are extremely poor and should not be taxed, but others, such as professionals or small manufacturing firms, should be required to pay taxes. We estimate that if just one quarter of current revenue losses from the informal sector were collected, this would bring in extra revenues of TShs 350 – 600 billion a year ($220 - 377 million).

The government is addressing several of the problems outlined in this report, notably by taking welcome steps to increase taxation of the informal sector. Yet its overall approach is insufficient to stem the large loss of potential revenue.

**The cost to Tanzanians**

Tax revenue losses mean less money available to be spent for development. In total, we estimate that Tanzania has in recent years been losing revenues ranging from $847 million - $1.29 billion (TShs 1.35 – 2.05 trillion) a year – thus the median figure is $1.07 billion (TShs 1.7 trillion). This figure is, however, an
under-estimate since it does not, for example, include tax revenue losses from other forms of unreported trade such as smuggling, for which no data are available. Neither does it include revenue losses from not fully taxing the informal sector.

Summary estimates of tax revenue losses

<table>
<thead>
<tr>
<th>Source of tax revenue losses</th>
<th>Low-end estimates of annual revenue loss</th>
<th>High-end estimates of annual revenue loss</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax exemptions for corporations (certificate holders with Tanzanian Investment Centre, mining sector, other private companies)</td>
<td>TShs 458.6 billion ($288 million)</td>
<td>TShs 458.6 billion ($288 million)</td>
</tr>
<tr>
<td>Illicit capital flows</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Of which trade mis-pricing</td>
<td>$28-198 million (TShs 45 – 315 billion)</td>
<td>$300 million (TShs 478 billion)</td>
</tr>
<tr>
<td></td>
<td>$33-38 million (TShs 53–61 billion)</td>
<td>$150 million (TShs 239 billion)</td>
</tr>
<tr>
<td>Mining sector alleged financial over-claims</td>
<td>$50 -100 million (TShs 80 – 160 billion)</td>
<td>$176 million (TShs 280 billion)</td>
</tr>
<tr>
<td>Company mis-reporting of sales and losses</td>
<td>TShs 240 billion ($151 million)</td>
<td>TShs 240 billion ($151 million)</td>
</tr>
<tr>
<td>Informal sector (revenue losses from the relatively non-poor who should be taxed)</td>
<td>TShs 350 billion ($220 million)</td>
<td>TShs 600 billion ($377 million)</td>
</tr>
<tr>
<td>TOTAL</td>
<td>$847 million (TShs 1.17 trillion)</td>
<td>$1.29 billion (TShs 2.06 trillion)</td>
</tr>
</tbody>
</table>

The loss of around $1.07 billion (TShs 1.7 trillion) amounts to over one sixth of the government’s entire budget expenditure of TShs 9.5 trillion in 2009/10. If the lost tax revenues were spent on education, the education budget would double; health spending would more than double and spending on agriculture – a massively under-funded sector – would more than triple. Alternatively, Tanzania could drastically reduce its reliance on foreign aid: the amount lost from taxes is over half the amount in aid received by Tanzania in 2009/10 (TShs 3.2 trillion).

Policy recommendations

The government should address tax revenue losses with a sense of urgency and take greater steps to increase revenue collections. Most importantly, it should:

- Undertake a review, to be made public, of all tax incentives with a view to reducing or removing many of them. The aim should be to remove most of the incentives granted to the mining sector and reduce or remove many of those granted in the EPZs. What tax incentives remain should be linked to performance requirements for sectors, such as employment creation and technology transfer.

- Provide annually, during the budget process, a publicly available tax expenditure analysis, showing the cost to the government of the various tax incentives and the beneficiaries.

- Review the Mining Act of 2010 to remove the possibility to provide companies with fiscal stabilisation clauses. Renegotiate the terms of all mining agreements with individual companies, to bring them into line with Tanzanian legislation and ensure that fair taxes are paid. Make all individual mining agreements public.
• Review fiscal policy for the oil and gas sector to ensure that tax terms are fair, that agreements are subject to public scrutiny and that Production Sharing Agreements optimally benefit the people of Tanzania.

• Go beyond the provisions of the voluntary Extractive Industries Transparency Initiative (EITI) scheme and introduce legislation to compel all foreign companies operating in Tanzania to provide details of their tax payments to the Tanzanian government and make this information publicly available.

• Undertake an analysis, to be made public, of the extent of trade mis-pricing in Tanzania

• Government and mining companies become transparent about tax and non tax contributions made at all various levels of government from village to the central level

• Increase training of officials to recognise transfer pricing, distinguish between legal and illegal forms of transfer pricing, and capital flight issues in key sectors, such as mining, and build a stronger capacity to respond to the problem. Take steps to ensure implementation of the requirement by companies to provide to the TRA details of their company sales pricing. Ensure that the requirement under Tanzanian legislation for associate companies to trade at arm’s length is implemented.
Introduction

This report analyses Tanzania’s tax policies and how much revenue the country is losing from tax evasion, capital flight and tax incentives for companies provided by the government. Tanzania is extremely poor, with its 45 million people living on average incomes of just $530 a year. Yet our study shows that, every year, a vast amount of potential tax revenue that could be used to reduce poverty is failing to end up in the government treasury; much is simply leaving the country.

Increasing the revenues available to the government is especially critical during the current global financial crisis when countries are even more vulnerable to shocks. In January 2010, for example, the Tanzanian government sought assistance to shore up the country’s finances after severe power and food shortages nearly emptied the government’s purse. At this stage, foreign reserves had shrunk to around $3.9 billion, equivalent to only six months worth of imports.

The issue of fair taxes is also vital in light of future income from Tanzania’s recently-discovered oil and natural gas – reserves of the latter alone are worth around $150 billion, six times the country’s national wealth (GDP). But this is the potential not actual revenues. How these potential revenues from oil and gas will be divided in future may well decide whether Tanzania significantly reduces poverty or not.

Although the government is taking some steps to improve tax revenue collections, Tanzania needs a fresh, more radical approach to raising sufficient tax revenues, especially as regards the businesses operating in the country. It is hoped that this report, which makes several recommendations to the government, will help
in this process. Developing an effective tax system in Tanzania is vital not only since it can generate increased revenues for the government to invest in social and economic development in order to eradicate poverty. But also, effective tax systems can help countries escape dependence on foreign aid or on a single natural resource, thus helping to diversify a country’s economic base. Just as critical is the role that an effective tax system can play in promoting democracy – by reinforcing the legitimacy of the government and promoting the accountability of the government to its citizens. How well government money is spent is a sign of how deep a democracy really is. And how fairly government revenues are raised is a sign of how equitable a society’s development is.

### Box 1: Poverty and inequality in Tanzania

- Average annual incomes: $530
- Proportion of people living on less than $1.25 a day: 33 per cent
- Life expectancy at birth: 57 years
- Literacy rate: 73 per cent
- Proportion of total expenditure on consumption by richest fifth of households: 42 per cent; poorest fifth: 7 per cent.

### Exchange rate

An exchange rate of US$ 1 = TShs 1,593 – prevailing in March 2012 - has been used in this report.
1. Taxes in Tanzania

We first outline what taxes, and how much, are collected in Tanzania before turning briefly to who pays them.

1.1 Taxes collected in Tanzania

Tanzania collected TShs 4.0 trillion (§2.5 billion) in taxes in 2008/09 (table 1) and TShs 4.5 trillion (§2.8 billion) in 2009/10 (table 2). Of these, around 30 per cent came each from Value Added Tax (VAT) and income tax while excise duties accounted for around 18 per cent and import duties for around 9 per cent. These taxes are collected by the Tanzania Revenue Authority (TRA), established in 1995, which also administers, assesses and accounts for revenues due under Tanzania’s tax laws. The TRA employs nearly 4,000 staff and consists of four revenue departments – the Tax Investigation Department, the Large Taxpayers Department, the Domestic Revenue Department and the Customs and Excise Department.5

Table 1: Government tax revenues, 2004/05 – 2010/11

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total domestic revenue</td>
<td>1,773,573.4</td>
<td>2,124,843.7</td>
<td>2,759,022.4</td>
<td>3,634,580.6</td>
<td>4,240,074.3</td>
<td>5,096,016.3</td>
<td>4,688,335.3</td>
<td>6,003,589.9</td>
</tr>
<tr>
<td>A. Tax revenue</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Import Duty</td>
<td>103,570.0</td>
<td>190,855.8</td>
<td>242,831.8</td>
<td>289,375.6</td>
<td>359,255.3</td>
<td>410,088.7</td>
<td>407,838.7</td>
<td>465,859.8</td>
</tr>
<tr>
<td>2. Excise Duty</td>
<td>237,850.7</td>
<td>261,530.3</td>
<td>320,078.1</td>
<td>660,888.2</td>
<td>762,092.7</td>
<td>973,320.6</td>
<td>894,411.6</td>
<td>1,062,925.8</td>
</tr>
<tr>
<td>3. Value Added Tax</td>
<td>681,036.1</td>
<td>803,024.6</td>
<td>821,627.9</td>
<td>1,042,489.7</td>
<td>1,231,135.4</td>
<td>1,474,470.9</td>
<td>1,330,179.6</td>
<td>1,860,585.8</td>
</tr>
<tr>
<td>4. Income Tax</td>
<td>446,838.0</td>
<td>554,048.0</td>
<td>716,320.5</td>
<td>983,804.8</td>
<td>1,228,645.8</td>
<td>1,428,419.9</td>
<td>1,333,834.1</td>
<td>1,642,588.6</td>
</tr>
<tr>
<td>5. Other Taxes</td>
<td>145,900.1</td>
<td>136,954.0</td>
<td>218,281.1</td>
<td>382,792.0</td>
<td>462,543.8</td>
<td>552,576.7</td>
<td>487,789.5</td>
<td>606,460.4</td>
</tr>
<tr>
<td>B. Nontax revenue</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Parastatal</td>
<td>12,587.1</td>
<td>13,232.2</td>
<td>10,567.5</td>
<td>58,253.5</td>
<td>25,865.9</td>
<td>25,597.0</td>
<td>17,917.9</td>
<td>32,179.6</td>
</tr>
<tr>
<td>2. Ministries and regions</td>
<td>106,025.3</td>
<td>124,642.3</td>
<td>131,080.1</td>
<td>172,793.7</td>
<td>153,334.3</td>
<td>201,706.7</td>
<td>196,878.7</td>
<td>302,800.7</td>
</tr>
<tr>
<td>3. Other nontax revenue</td>
<td>36,676.1</td>
<td>46,536.7</td>
<td>67,935.4</td>
<td>44,280.0</td>
<td>15,200.9</td>
<td>27,835.7</td>
<td>19,485.0</td>
<td>30,016.4</td>
</tr>
</tbody>
</table>

Source: MOF, Budget Digest 2010/11, June 2010, Table 3

A more detailed breakdown of tax revenues, from figures provided in the 2011/12 budget, is provided in Table 2.
### Table 2: Government tax revenues 2009/10 – 2010/11

<table>
<thead>
<tr>
<th></th>
<th>2009/10 Actual collection (Billion TShs)</th>
<th>2010/11 Approved estimates (Billion TShs)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Taxes on international trade</strong></td>
<td>1,979</td>
<td>2,476</td>
</tr>
<tr>
<td>Of which:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>VAT on imports</td>
<td>748</td>
<td>874</td>
</tr>
<tr>
<td>Excise duty on imports</td>
<td>533</td>
<td>741</td>
</tr>
<tr>
<td>Import duty</td>
<td>374</td>
<td>535</td>
</tr>
<tr>
<td>Fuel levy</td>
<td>256</td>
<td>303</td>
</tr>
<tr>
<td>Other</td>
<td>68</td>
<td>23</td>
</tr>
<tr>
<td><strong>Taxes on income, profits and capital gains</strong></td>
<td>1,250</td>
<td>1,673</td>
</tr>
<tr>
<td>Of which:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PAYE from government, parastatal and private sector employees (non-large taxpayers)</td>
<td>267</td>
<td>285</td>
</tr>
<tr>
<td>PAYE from government, parastatal and private sector employees (large taxpayers)</td>
<td>433</td>
<td>663</td>
</tr>
<tr>
<td>Limited companies (non-large taxpayers)</td>
<td>95</td>
<td>115</td>
</tr>
<tr>
<td>Limited companies (large taxpayers)</td>
<td>319</td>
<td>424</td>
</tr>
<tr>
<td>Withholding taxes (non-large taxpayers)</td>
<td>37</td>
<td>22</td>
</tr>
<tr>
<td>Withholding taxes (large taxpayers)</td>
<td>84</td>
<td>124</td>
</tr>
<tr>
<td>Individuals – Presumptive and assessed tax (non-large taxpayers)</td>
<td>50</td>
<td>60</td>
</tr>
<tr>
<td>Individuals – Assessed tax (large taxpayers)</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Capital gains tax (non-large taxpayers)</td>
<td>6</td>
<td>12</td>
</tr>
<tr>
<td>Capital gains tax (large taxpayers)</td>
<td>6</td>
<td>0</td>
</tr>
<tr>
<td>Unclassified income tax refund (non-large taxpayers)</td>
<td>-51</td>
<td>-57</td>
</tr>
<tr>
<td>Others</td>
<td>3</td>
<td>25</td>
</tr>
<tr>
<td>Payroll and skills development levy</td>
<td>108</td>
<td>130</td>
</tr>
<tr>
<td><strong>Taxes on goods and services</strong></td>
<td>967</td>
<td>1,221</td>
</tr>
<tr>
<td>Of which:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value Added Tax (non-large taxpayers)</td>
<td>159</td>
<td>225</td>
</tr>
<tr>
<td>Value Added Tax (large taxpayers)</td>
<td>501</td>
<td>554</td>
</tr>
<tr>
<td>Excise duty (large taxpayers)</td>
<td>299</td>
<td>438</td>
</tr>
<tr>
<td>Others</td>
<td>8</td>
<td>4</td>
</tr>
<tr>
<td>Motor vehicle taxes/fees</td>
<td>85</td>
<td>72</td>
</tr>
<tr>
<td>Others</td>
<td>67</td>
<td>80</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>4,456</td>
<td>5,652</td>
</tr>
</tbody>
</table>

Source: MOF, Financial Statement and Revenue Estimates, 2011/12 Budget, Vote 21, www.mof.go.tz. Nb. Figures have been rounded from the original.

The figures above are tax revenues accruing to the Treasury only. They do not include the following revenues from royalty and dividend payments:
Table 3: Royalty and dividend payments, 2009/10

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Royalties and fees paid by the mining sector to the Ministry of Energy and Minerals</td>
<td>TShs 61.9 billion</td>
</tr>
<tr>
<td>Dividends from public and private enterprises and parastatal institutions paid to the Ministry of Finance (such as by the Consolidated Holdings Corporation, Tanzania Cigarettes Company and Tanzania Breweries Ltd)</td>
<td>TShs 16.2 billion</td>
</tr>
<tr>
<td>Forest royalties paid to the Ministry of Natural Resources and Tourism</td>
<td>TShs 29.8 billion</td>
</tr>
<tr>
<td>Export royalties and fishing licence fees paid by fishing companies to the Ministry of Livestock Development and Fisheries</td>
<td>TShs 5.9 billion</td>
</tr>
</tbody>
</table>

Source: MOF, Financial Statement and Revenue Estimates, 2011/12 Budget, various votes, mof.go.tz

Local Government Authorities have the power to raise funds by imposing various taxes and levies on businesses in their areas but after various reforms, they now raise less than 10 per cent of their revenues locally, while the rest is funded by central government. This proportion has declined in recent years despite governments’ pursuit of greater decentralisation in Tanzania. The most important taxes raised locally are those on local business activity, notably the ‘produce cess’ (turnover taxes on agricultural production which are supposed to be up to 5 per cent of farmgate prices) and the service levy (a turnover tax of 0.3 per cent for firms with turnover in excess of TShs 20 million). The government forecasts that it will collect only TShs 350 billion ($220 million) from local authorities in 2011/12, out of total tax collections of TShs 6.2 trillion ($3.9 billion).

Table 4: Main sources of Local Government Authorities revenues

<table>
<thead>
<tr>
<th>Local Taxes</th>
<th>Asset / Property Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Property / Building Tax</td>
</tr>
<tr>
<td></td>
<td>Land Rent</td>
</tr>
<tr>
<td>Product / Sales Tax</td>
<td></td>
</tr>
<tr>
<td>Crop Cess (maximum 5% of farm gate price). NB: Proposed in the 2009/10 budget to be 3% from the 2010/11 financial year</td>
<td></td>
</tr>
<tr>
<td>Livestock Auction fee (to be charged only within the market and livestock actually sold)</td>
<td></td>
</tr>
<tr>
<td>Service Levy</td>
<td></td>
</tr>
</tbody>
</table>
1.2 Who pays the taxes? The narrow tax base

Tanzania has a narrow tax base, which reduces potential revenues and makes the country more dependent than it could be on a small section of society. The TRA states that 400 large taxpayers (handled by the TRA’s Large Taxpayers Department) account for 70 per cent of domestic revenue collections (excluding trade-related taxes) and that small and medium-sized taxpayers account for the remaining 30 per cent.9 The informal sector accounts for 40-60 per cent of GDP10 and around 70 per cent of the country’s workforce11 but is largely untaxed. The informal sector includes extremely poor small farmers and urban petty traders, who arguably should not be taxed at all. Yet it also includes wealthier people and businesses such as professionals and small manufacturers who often pay little or no tax.12 These individuals and small businesses should be captured in the tax net in order to increase government revenues (see section 4.4).

Thus the number of individuals who pay tax in Tanzania is low: According to the TRA, only 1.6 million out of a potential 15 million people pay taxes.13 However, it is worth noting that there has been an increase in the number of registered taxpayers in recent years. By June 2011, there were around 846,000 Tax Identification Number (TIN) registered income taxpayers, compared to 289,000 in 2006, and 17,000 registered VAT taxpayers, compared to 6,000 in 2006.14 It is also worth noting, however, that being registered as a taxpayer does not always translate into actually paying tax. For example, the process of acquiring a new driving licence requires drivers to be TIN-registered, but not all holders of driving licences are actually paying tax.
1.3 Tax collections as a proportion of GDP

The IMF outlines Tanzania’s tax collections as follows:

Table 5: Tax revenue as percentage of GDP (actual collections)\(^5\)

<table>
<thead>
<tr>
<th></th>
<th>2005/06</th>
<th>2006/07</th>
<th>2007/08</th>
<th>2008/09</th>
<th>2009/10</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>11.4</td>
<td>13.0</td>
<td>14.7</td>
<td>15.3</td>
<td>14.6</td>
</tr>
</tbody>
</table>

Tanzania’s tax collections have increased over the years. The TRA states, for example, that revenue collections increased in absolute terms from $1.6 billion in 2004 to $3.7 billion in 2009/10.\(^6\) Indeed, they averaged only 11 per cent of GDP throughout the 1990s.\(^7\) However, the World Bank notes that domestic revenues in Tanzania are below the average for sub-Saharan Africa and ‘not high by international standards’.\(^8\) In recent years, collections have been static at around 15 per cent of GDP. By comparison, taxes bring in 19 per cent of GDP in neighbouring Kenya and 11.8 per cent in Uganda.\(^9\) In OECD countries, the proportion is around 30 per cent.\(^10\) Indeed, Tanzania suffers from a significant ‘tax gap’ (see Box 2).
Box 2: Tanzania’s ‘tax gap’ according to the IMF

The IMF estimates that Tanzania has a potential tax revenue of 20.9 per cent of GDP. This means that its ‘tax gap’ – the difference between actual and potential revenue collections – was a massive 6.3 per cent of GDP in 2009/10, amounting to around TShs 1.9 trillion. This is due to the failure to collect all taxes from the informal sector and to the large revenue losses from providing tax exemptions.

<table>
<thead>
<tr>
<th></th>
<th>2008/09</th>
<th>2009/10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax revenue collected as percentage of GDP</td>
<td>15.3</td>
<td>14.6</td>
</tr>
<tr>
<td>Tax revenue potential as percentage of GDP</td>
<td>20.9</td>
<td>20.9</td>
</tr>
<tr>
<td>Tax gap in percentage</td>
<td>5.6</td>
<td>6.3</td>
</tr>
<tr>
<td>Tax gap in Billion TShs</td>
<td>1,484</td>
<td>1,910</td>
</tr>
</tbody>
</table>

Sources: IMF, Staff Report for the 2011 Article IV Consultation and Second Review under the Policy Support Instrument, 21 April 2011, p.25; Tax gap in TShs is based on GDP figures of TShs 30,321 billion in 2009/10 and TShs 26,497 in 2008/09.

Based on projected GDP figures, Tanzania’s tax gap will amount to 4.8 per cent of GDP in 2010/11, meaning revenue losses of TShs 1,668 billion.

The IMF’s ‘tax gap’ calculation noted above includes only losses from tax exemptions and the informal sector; it does not include revenue losses from tax avoidance, tax evasion or trade mis-pricing, for example. We now turn to these ways in which Tanzania is losing badly-needed tax revenues, looking first at tax incentives.
2. Tax incentives and revenue losses

Tanzania provides a vast array of tax incentives and exemptions to foreign and domestic companies and institutions. Of particular concern to this analysis is the range of tax incentives given to companies supposedly to attract foreign investment, such as income tax holidays and exemptions from import duties, which, although legal, are unnecessarily depriving the country of revenues.

**Box 3: What are tax exemptions and incentives?**

A tax incentive is defined as ‘a deduction, exclusion or exemption from a tax liability, offered as an enticement to engage in a specified activity such as investment in capital goods for a certain period’. Tax incentives include corporate income tax holidays and reductions in tax rates, and are granted to attract foreign and at times domestic investment and/or to promote specific economic policies, such as to encourage investment in certain sectors. Tax incentives are often accompanied by other, non-tax incentive policies that further aim at luring investors to specific locations like export processing zones, or to specific sectors such as mining and agriculture.

**Tax incentives to encourage investment**

**Corporate tax incentives**
- Tax holidays or reduced tax rates
- Tax credits
- Investment allowances
- Accelerated depreciation
- Reinvestment or expansion allowances

**Other tax incentives**
- Exemption from or reduction of withholding taxes
- Exemption from import tariffs
- Exemption from export duties
- Exemption from sales, wage income or property taxes
- Reduction of social security contributions

**Financial and regulatory incentives**
- Subsidised financing
- Grants or loan guarantees
- Provision of infrastructure, training
- Preferential access to government contracts
- Protection from import competition
- Subsidised delivery of goods and services
- Derogation from regulatory rules and standards
2.1 Tax incentives to investors

The major tax incentives provided to companies in Tanzania are outlined in Box 4 (see Annex for a more detailed list).

**Box 4: Major tax incentives for companies operating in Tanzania**

**For all holders of Tanzania Investment Centre Certificate of Incentives:**
- import duty exemption on project capital goods for investment in lead sectors, including agriculture, mining and infrastructure
- zero per cent VAT on inputs for mining, agriculture, tourism and goods manufactured for export
- 100 per cent capital allowance on industrial plant, buildings and machinery and on agricultural expenditure

**For investors in the Export Processing Zones:**
- exemption for the first 10 years from corporate income tax, withholding tax on rent, dividends and interest and all taxes imposed by Local Government Authorities
- import duty exemptions on raw materials and capital goods imported for manufacturing goods in the EPZs

**For those with ‘Strategic Investor Status’** (i.e., companies investing more than $20 million): companies can request specific incentives and have an individual fiscal agreement with the government. Thus mining companies have individual agreements with the government that offer them fiscal incentives and usually involve tax stabilisation clauses (meaning that if the government enacts higher taxes through general legislation, the companies will still retain their fiscal incentives and lower tax rates).

**For mining companies:**
- zero import duty on fuel and on imports of mining-related equipment during prospecting and up to the end of the first year of production
- exemption from paying capital gains tax
- special VAT relief, which includes exemption from VAT on imports and local supplies of goods and services to mining companies and their subcontractors
- 100 per cent capital allowance on all capital equipment (like machinery or property)

**For agricultural investors:**
- zero-rated duty on capital goods and all farm inputs
- reduced import tariff on project capital items to zero percent
- deferment of VAT payment on project capital goods
- import duty drawback on raw materials for inputs for export
- zero-rated VAT on agricultural exports and domestically produced agricultural inputs
Table 6 shows that the government has granted tax exemptions worth an average of **TShs 816 billion ($512 million)** each year in the three years 2008/09 – 2010/11. The main beneficiaries are companies holding certificates with the Tanzania Investment Centre, mining companies and other private companies: together, they account for 56 per cent of all exemptions. Mining companies benefitted from exemptions worth TShs 72.6 billion ($45.6 million) a year.

Table 6: Tax exemptions granted by government to institutions, 2008/09 – 2010/11 (Billion TShs)

<table>
<thead>
<tr>
<th></th>
<th>2008/09</th>
<th>2009/10</th>
<th>2010/11</th>
<th>Average over the 3 years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government institutions</td>
<td>21.6</td>
<td>52.7</td>
<td>35.9</td>
<td>36.7</td>
</tr>
<tr>
<td>Parastatal organisations</td>
<td>7.1</td>
<td>8.8</td>
<td>8.1</td>
<td>8.0</td>
</tr>
<tr>
<td>Religious institutions</td>
<td>0.4</td>
<td>0.3</td>
<td>1.6</td>
<td>0.8</td>
</tr>
<tr>
<td>NGOs</td>
<td>37.2</td>
<td>25.5</td>
<td>22.1</td>
<td>28.3</td>
</tr>
<tr>
<td>Donor funded projects</td>
<td>21.6</td>
<td>115.8</td>
<td>72.5</td>
<td>70.0</td>
</tr>
<tr>
<td>Private companies and individuals</td>
<td>51.2</td>
<td>182.7</td>
<td>36.2</td>
<td><strong>90.0</strong></td>
</tr>
<tr>
<td>Mining sector</td>
<td>59.1</td>
<td>109.9</td>
<td>48.7</td>
<td>72.6</td>
</tr>
<tr>
<td>Tanzania Investment Centre</td>
<td>380.1</td>
<td>239.7</td>
<td>268.0</td>
<td><strong>296.0</strong></td>
</tr>
<tr>
<td>VAT exemptions</td>
<td>170.1</td>
<td>279.8</td>
<td>168.7</td>
<td><strong>206.2</strong></td>
</tr>
<tr>
<td>Duty free shops exemptions</td>
<td>3.9</td>
<td>17.4</td>
<td>2.7</td>
<td><strong>8.0</strong></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>752.4</td>
<td>1,016.3</td>
<td>680.7</td>
<td><strong>816.5</strong></td>
</tr>
</tbody>
</table>


Other sources give slightly different figures for the amount of exemptions provided. For example, a 2011 IMF report estimates that tax exemptions cost the government 3.5 per cent of GDP per year. Our calculation is that this would amount to TShs 1.06 trillion in 2009/10. A report for the African Development Bank (AfDB) gives an even higher estimate, noting that exemptions and incentives account for up to 6 per cent of GDP, or TShs 1.8 trillion in 2008 - though it is unclear how the AfDB arrived at this figure or how 6 per cent translates into Tsh 1.8 trillion. Tax exemptions as a proportion of GDP have been around 2.9 per cent in recent years.

Our view is that all these tax exemptions are of concern but that those granted to corporations (ie, certificate holders with the Tanzania Investment Centre, mining companies and other private companies) represent an especially unnecessary loss of revenue (see further section 2.4). Exemptions given to these corporations have deprived Tanzania of an average of **TShs 458.6 billion ($288 million)** a year in the three years 2008/09 – 2010/11.
Box 5: Missing: Some of the largest companies

In August 2011, Prime Minister Mizengo Pinda outlined to parliament 15 companies regarded as being the best taxpayers in the country for the past five years. But the list left out many large companies, including all mining companies except Resolute - the smallest foreign mining firm in the country – and all telecommunications firms except Airtel - the second in terms of market share. The non-appearance of many large companies raises the concern that they are paying few taxes because of the large tax incentives given to companies in Tanzania.

The companies listed by the prime minister were:

- Tanzania Breweries Ltd (which paid taxes of TShs 65.4 billion during 2005-2011)
- National Microfinance Bank (TShs 108.6 billion)
- Tanzania Cigarette Company (TShs 92.1 billion)
- National Bank of Commerce (TShs 89.9 billion)
- CRDB Bank Ltd (TShs 79.2 billion)
- Tanzania Ports Authority (TShs 76.8 billion)
- Tanzania Portland Cement (TShs 73.4 billion)
- Airtel (Tanzania) Ltd (TShs 63.6 billion),
- Tanga Cement Company Ltd (TShs 43.6 billion)
- Standard Chartered Bank Ltd (TShs 40 billion)
- Citibank Tanzania Ltd (TShs 35.7 billion)
- Resolute Tanzania Ltd (TShs 32.1 billion)
- Tanzania International Container Terminal Services (TShs 25.9 billion)
- Tanzania Distillers Ltd (TShs 13.4 billion)
- Group Five International (PTY) Ltd. (TShs 9.5 billion)

2.2 Tax Incentives in the mining sector

Although Tanzania is one of Africa’s largest gold producers - and gold exports have risen from around US$500 million to US$1.5 billion in the last five years due to rising gold prices - government revenues from mining have remained at only around US$100 million a year (see Box 6).
Box 6: How much are mining companies paying in tax?

Historically, mining companies have paid very little tax. Presently, the IMF notes that they pay around $100 million a year in all taxes which is equivalent to less than 7 per cent of the value of mineral exports. Lower figures are provided by the Tanzania Minerals Audit Agency (TMAA), which states that the six major gold mines paid $80.6 million in 2008.

<table>
<thead>
<tr>
<th>Royalty payments by major gold mines (in $ million)</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>6.9</td>
<td>11.0</td>
<td>14.1</td>
<td>18.3</td>
<td>15.8</td>
<td>17.1</td>
<td>22.1</td>
<td>24.4</td>
<td>29.2</td>
<td>40.5</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Other taxes paid by all large-scale miners (in $ million)</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>15.5</td>
<td>20.1</td>
<td>21.3</td>
<td>19.2</td>
<td>33.1</td>
<td>17.7</td>
<td>27.5</td>
<td>56.2</td>
<td>na</td>
<td>na</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>TOTAL TAXES PAID (in $ million)</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>25.4</td>
<td>31.1</td>
<td>35.4</td>
<td>37.5</td>
<td>58.9</td>
<td>34.8</td>
<td>49.6</td>
<td>80.6</td>
<td>na</td>
<td>na</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Value of gold exports (in $ million)</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>294</td>
<td>424</td>
<td>571</td>
<td>600</td>
<td>551</td>
<td>756</td>
<td>781</td>
<td>903</td>
<td>1,095</td>
<td>1,485</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Taxes paid as % of gold exports</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>8.6</td>
<td>7.3</td>
<td>6.2</td>
<td>6.2</td>
<td>10.7</td>
<td>4.6</td>
<td>6.3</td>
<td>8.9</td>
<td>na</td>
<td>na</td>
</tr>
</tbody>
</table>

NB: Other taxes include corporate income tax, VAT, Pay As You Earn (PAYE), Skills Development Levy and Withholding Tax. The ‘other taxes’ paid include those by all large-scale miners, but which are overwhelmingly gold mining companies.

Source: TMAA, Annual Report 2010, pp.30-31

It should be noted that most of the tax paid in the mining sector is by employees of the companies, in the form of Pay As You Earn (PAYE), not by the companies themselves. In 2008, for example, 65 per cent of all the tax paid by large-scale miners was PAYE:

Figure 1: Taxes paid by large-scale mining companies 2008

Source: TMAA, Annual Report 2010, p.31

If PAYE accounts for 65 per cent of mining sector taxes, then the companies themselves are only paying around $35 million a year, using the $100 million total estimate of the IMF. This amount would more than double if the tax exemptions accorded to mining companies (worth $45.6 million) were removed.
Mining companies are paying few taxes mainly because of the tax incentives provided to them (see Box 7). The IMF noted in April 2011 that no gold companies had paid ‘material income tax to date’. Later in 2011, however, it was reported that both Resolute and AngloGold Ashanti had started to pay corporate income tax for the first time. Yet mining revenues are not likely to grow much in the near future. According to the IMF: ‘The growing mining sector has so far had little net fiscal impact and this is unlikely to change in the coming years, partly because of large embedded tax holidays... Net increases in revenue will be relatively small in the near term because of the offsetting impact of accumulated VAT and fuel tax refund claims’.

Box 7: Tax incentives for mining companies – Two examples

- Mining companies’ ability to offset against their taxable income the full costs of their expenditure on items such as plant and machinery has long lead to the declaration of tax losses, and thus non-payment of corporate income tax. In response to this the government introduced in 2008 an Alternative Minimum Tax of 0.3 per cent of turnover, payable when companies declare three consecutive years of tax losses, although it is likely that revenues from this tax are far lower than the losses caused by the capital allowance.

- The Bomani Commission established by the government estimated that the country lost TShs 39.8 billion in 2006/7 and TShs 59 billion in 2007/8 simply as a result of fuel levy exemptions granted to the six large mining companies. As of late 2011, mining companies were making claims to the government for refunds totaling US$274 million related to their fuel levy exemptions for the period since 2002.

A new mining act was passed in 2010, the product of the Mining Sector Review Committee commissioned by the President and chaired by a former Attorney-General, Mark Bomani. The Committee was a response to incessant public outcries that the 1998 Mining Act simply did not benefit Tanzania. The new Act brings some important changes to the mining sector: notably, it increases the royalty rate for gold from 3 to 4 per cent, it allows government to own stakes in mining operations and it reserves future diamonds and gemstone mining for Tanzanians. However, the Act in effect applies only to new projects, since existing gold mines remain governed by the generous fiscal terms and tax stabilisation clauses outlined in individual mineral development agreements. In June 2011, for example, it was reported that the government was considering levying a ‘super profits tax’ on windfall earnings from mining. But AngloGold Ashanti, which operates the country’s largest gold mine, stated that the introduction of such a tax would not affect its tax payments since its mining agreement with the government has a fiscal stabilisation clause, forbidding the government from raising taxes on the company without paying compensation. Without changes to the fiscal terms of these agreements, Tanzania is unlikely to generate significantly increased mining revenues.

2.3 Problems with tax incentives

The evidence suggests that the disadvantages of tax incentives vastly outweigh the advantages and that such incentives are generally not needed to attract foreign direct investment (FDI). Proponents of tax incentives often argue that lower tax burdens give investors a higher net rate of return and increase income for re-investment; the host country thus attracts increased FDI, income and the transfer of technology. A further argument is that incentives are needed to offset the otherwise poor investment climate: undeveloped infrastructure, the high cost of doing business, the macroeconomic instability and corruption. However, there are numerous disadvantages with tax incentives: they not only reduce revenues but they can require large administrative resources, can encourage corruption, can encourage footloose firms who invest and divest quickly, and can be provided in a non-transparent way.
The IMF notes that if investment incentives are to be of benefit, they should be well-targeted and focused narrowly on the activities they seek to promote but that ‘the corporate income tax holiday usually does not meet the criterion of a well-targeted incentive’. Tax holidays strongly favour transitory rather than sustainable investments and create glaring opportunities for aggressive tax avoidance. Generally, investment incentives are recommended when the business is a public good, such as projects for encouraging green technologies, primary health care and disease prevention, and research and development. Although some tax incentives can be justified to attract foreign investment, evidence suggests that generally tax incentives are not needed to do so. A 2006 report by the African Department of the IMF, focusing on tax incentives in East Africa, notes that ‘investment incentives – particularly tax incentives – are not an important factor in attracting foreign investment’. Countries that have been most successful in attracting foreign investors have not offered large tax or other incentives. A large body of literature shows that more important factors in attracting foreign investment are good quality infrastructure, low administrative costs of setting up and running businesses, political stability and predictable macro-economic policy. Indeed, this reasoning partly explains why the IMF, and other international organisations such as the African Development Bank, have been pressing Tanzania, and other governments in East Africa, to radically reduce their tax exemptions (see section 6.2).

The tax incentives granted by Tanzanian governments appear overly generous, despite recent government pledges to reduce some of them (see section 6.2). The suspicion remains that the principal reason for retaining significant tax exemptions is political, in order to favour certain sectors and companies.
THE ONE BILLION DOLLAR QUESTION: How Can Tanzania Stop Losing So Much Tax Revenue

Box 8: Are tax exemptions losing more revenue than Export Processing Zones create?

The government claims that tax and other incentives offered to investors in the EPZs are necessary to attract foreign direct investment. But the key question is whether the extent of tax exemptions is justified in terms of the amount of foreign investment that results. Our analysis in the section above is that the tax exemptions given to corporations are depriving Tanzania of an average of TShs 458.6 billion ($288 million) a year. Many of these exemptions apply to EPZs, although exact figures are not known. According to government figures the EPZs have resulted in investments worth $710 million since 2002. Comparing the two figures means that Tanzania has lost more revenues from tax exemptions given to corporations in the last three years than it has received in all foreign investment since the EPZs were established. Furthermore, foreign investment is clearly not the same thing as revenues, meaning that the actual difference is far greater.

Other analyses also cast doubt on the benefits of the EPZs in attracting foreign investment. A 2009 analysis by the UN trade body, UNCTAD, found that the economic contribution of the EPZ programme was ‘insignificant in terms of the size of investments, jobs created and value and volume of exports’; the study estimated that investments were then around $247 million. A 2006 IMF report covering East Africa noted that the introduction of EPZs in 2002 ‘has not resulted in a noticeable pickup in foreign investment’ in Tanzania. It noted that Uganda had continued to attract higher levels of foreign investment than Tanzania without providing such generous investment incentives. Table 7 shows that foreign investment in Tanzania has not significantly increased in recent years.

Table 7: Foreign investment flows to East Africa ($ million)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kenya</td>
<td>51</td>
<td>729</td>
<td>96</td>
<td>141</td>
<td>133</td>
</tr>
<tr>
<td>Tanzania</td>
<td>597</td>
<td>647</td>
<td>679</td>
<td>645</td>
<td>700</td>
</tr>
<tr>
<td>Uganda</td>
<td>644</td>
<td>792</td>
<td>729</td>
<td>816</td>
<td>848</td>
</tr>
</tbody>
</table>

Source: UNCTAD, World Investment Report 2011, Annex Table 1.1

The EPZs are meant to play a critical role in helping to achieve the target, set by Tanzania’s Development Vision 2025, of exports accounting for 25 per cent of GDP by 2025. Yet with the EPZ scheme in place for nearly a decade, exports currently amount to only $410 million or around 2 per cent of GDP. Joint ventures in EPZ firms between Tanzanians and foreigners have been difficult to forge, mainly because the former lack adequate managerial and technical skills and access to capital. As a result, technology and know-how transfer have so far been limited. Tanzania’s EPZ Authority claims that EPZ firms have so far created 15,100 jobs. Yet this means that one job has been created for every $47,000 invested – a low number. Indeed, the evidence is that EPZ firms have continued to rely on expatriates, especially for advanced technology-related skills. There are also major problems with poor labour conditions, an issue widely documented in EPZs in Africa and around the world. Indeed, it may be low wages and weaker regulations, including the banning of unions, that attracts investors more than tax exemptions.
2.4 Regional tax competition

Tanzania’s provision of tax incentives is part of the tax competition among the members of the East African Community (EAC). Following the EAC’s establishment in 1999, Kenya, Tanzania and Uganda created a customs union (a duty-free trade area with a common external tariff) in 2005, and were joined by Rwanda and Burundi in 2009. This has created a larger regional market, and means that firms can be located in any EAC country to service this market. At the same time, however, countries are being tempted to increase investment incentives in order to attract FDI and, they believe, increase jobs and exports. As a 2006 IMF report notes:

‘Increased competition over FDI and growing pressure to provide tax holidays and other investment incentives to attract investors could result in a “race to the bottom” that would eventually hurt all three [ie, Kenya, Uganda and Tanzania] EAC members. Left unchecked, the contest could result in revenue loss, especially in Tanzania and Uganda, and threaten the objective of improving revenue collection.’

The wide range of tax incentives provided by Tanzania and its fellow member states in the EAC are leading to a ‘race to the bottom’. In both Kenya and Uganda, for example, governments are also granting massive tax incentives, partly in a competition to attract FDI, with the result being significant revenue losses for the government, as in Tanzania.

Tax competition can occur when firms are able to locate where tax rates are lowest, thereby encouraging other countries to lower their tax rates in order to retain and attract dynamic firms and able workers. Tax competition can make it difficult for countries to maintain desired tax rates, leading to ever-declining tax rates and revenues. Economic and Finance Ministers in the European Union have defined harmful tax competition as including factors such as: an effective level of taxation which is significantly lower than the general level of taxation in the country concerned; the presence of tax benefit categories reserved for non-residents; and tax incentives for activities which are isolated from the domestic economy and therefore have no impact on the national tax base.
3. Illicit capital flight and revenue losses

Further revenue losses in Tanzania are resulting from capital flight, which may be exacerbated by the problem of tax havens. Capital flight means money leaving the country but can be either legal or illegal. The legal variety includes investments or banking deposits made by companies abroad after paying the necessary taxes in Tanzania and is often caused by an anticipated devaluation of the currency. Thus these flows often follow macro-economic or political instability or the fear on the part of domestic investors of financial loss. This report, however, is concerned with the illegal variety of capital flight – also called illicit financial flows - which entails the deliberate disguised expatriation of money abroad, usually to developed countries or tax havens. This principally takes three forms:

- transactions arising from criminal activities such as the drugs trade
- corruption, such as the embezzlement of national wealth
- tax evasion by transnational corporations

The latter – tax evasion by TNCs - can itself take various forms and includes activities such as ‘trade mis-pricing’. Trade mis-pricing often involves a multinational company deciding the allocation of profits between its subsidiaries to reduce its tax liability; it does this by artificially inflating or deflating import or export prices for goods ‘traded’ between those subsidiaries in order to pay tax in the territory with lower tax rates (see Box 9).

**Box 9: What are transfer pricing and trade mis-pricing?**

**Transfer pricing** occurs when two related companies – a parent company and a subsidiary, or two subsidiaries controlled by a common parent – trade with each other. When the parties establish a price for the transaction, they are engaging in transfer pricing. Transfer pricing is not, in itself, illegal.

What is illegal or abusive is **trade mis-pricing**. This involves a company allocating profits between its subsidiaries and inflating or deflating import or export prices to reduce the taxable profits. The various forms of trade mis-pricing include **transfer mis-pricing** (where different parts of the same company sell goods or services to each other at manipulated prices) and **false invoicing** (where similar transactions take place between unrelated companies). These processes can also facilitate money laundering and can be used to disguise illegal commissions hidden in the inflated prices.

Trade mis-pricing is tax dodging, depriving countries of tax revenues, and for this reason is the focus of campaigns by many NGOs. Christian Aid, for example, has calculated that revenue losses to developing countries from two forms of trade mis-pricing – transfer mis-pricing and false invoicing - amount to around $160 billion a year. Total illicit capital flows are even greater since these include not only figures for trade mis-pricing but also for the proceeds of bribery, theft and tax evasion (what are often called ‘unrecorded capital leakages’). The US-based organisation, Global Financial Integrity (GFI) estimates that such illicit capital flows from all developing countries amounted to a massive $775–903 billion in 2009 and $1.26–1.44 trillion in 2008. Alleged trade mis-pricing by TNCs accounted for just over half the total.

Illicit capital flight amounts to stealing money from already poor countries. As a result of such capital flight, domestic resources available for financing public services are reduced. The tax loss from capital flight is likely to be greater than that from domestic tax evasion because in the case of domestic tax evasion the money
stays in the country and generates at least some tax revenue (for example sales tax or VAT when it is spent in the local economy) whereas capital that has fled offshore is not invested locally and does not generate local tax revenue.  

3.1 Illicit capital flows and Tanzania

As regards Tanzania, there are different estimates of the extent of illicit capital flight:

- In its 2011 global survey, Global Financial Integrity estimates that illicit capital flows from Tanzania amounted to between $937 million and $2.6 billion during 2000-9. These are low–end and high-end estimates, meaning an average yearly flow of between $94 and $257 million. Within the high-end estimate of $257 million a year, $127 million was from trade mis-pricing and $130 million was from ‘unrecorded capital leakages’.  

- In its 2010 review of illicit flows for the years 2002-06, GFI notes that Tanzania lost an average of $660 million a year (as the high-end estimate): $551 million as a result of unrecorded capital leakages and $109 million as a result of trade mis-pricing.  

- Another GFI report notes that during 2000-08 Tanzania lost $2.5 billion - an annual average of $278 million - and during 1970-2008 lost $7.36 billion from illicit capital flows.

These figures suggest that total illicit capital flows from Tanzania range from $94 – 660 million a year and that illicit flows from trade mis-pricing alone amount to $109 – 127 million a year. These are already very large figures but are likely to be gross under-estimates. Global Financial Integrity records the figures for various years as zero, owing to a lack of data: for example, the average figure for trade mis-pricing of $127 million, noted above, includes a figure of zero for four years alongside one year (2008) when Tanzania lost $440 million. Thus illicit capital flight is likely to be much greater. One expert working on this issue in Tanzania estimates that such flows could be close to $1 billion a year, with trade mis-pricing alone responsible for around $500 million.

Tax revenue losses from illicit capital flight are hard to calculate precisely given the lack of data. We make an assumption that these flows should have been subject to the prevailing corporate income rate of 30 per cent. Using the above figures from Global Financial Integrity, this means that total illicit flows cost the Tanzanian government $28–198 million and that trade mis-pricing causes annual revenue losses of $33–38 million. However, using the higher estimate of $1 billion in illicit capital flight produces tax revenue losses of $300 million a year, of which $150 million a year is from trade-mispricing.

Box 10: The problem of transfer mis-pricing in Tanzania

A senior TRA official informed the researchers that the TRA has undertaken a study of revenue losses from transfer pricing, but that the full report has not yet been made public. It is unclear whether the report comprehensively covers both transfer mis-pricing, which is illegal, and transfer pricing, which is legal. The official recognised that transfer pricing by transnational corporations is a very big, and increasing, problem in Tanzania with the potential for very large revenue losses. The TRA faces the problem of indentifying and capturing cases of transfer pricing, and being able to distinguish between legal and illegal practices. One challenge is to get all the necessary information from concerned companies. Another is the need to strengthen the TRA’s capacity to undertake investigations since few TRA staff understand transfer pricing techniques which are often complicated since they involve different countries and tax jurisdictions. (See also section 6.4)
3.2 Tax havens and Tanzania

Over half of world trade is now conducted through tax havens, half of all banking assets are held in offshore accounts and one third of foreign direct investment is channelled through offshore accounts.\textsuperscript{76} The use of tax havens is not illegal, but the secrecy afforded to transactions in these jurisdictions and entities established there allows vast amounts of money to be hidden from public scrutiny, and enables wealthy companies and individuals to avoid and evade paying taxes. Many transnational corporations have complex corporate structures involving several subsidiaries and holding companies, including in tax havens. A recent analysis surveyed 95 of the largest quoted companies in the UK, the Netherlands and France and found that all but one had subsidiaries in tax havens, the most popular being the Cayman Islands.\textsuperscript{77} The use of tax havens generally increases the possibility both of perfectly legal (but still often ethically questionable) tax avoidance and also of illicit capital flight.

Our research has found that many of the largest companies operating in Tanzania use tax havens in their corporate structures (see Box 11). We are making no accusations against specific companies, however. The list in Box 11 is illustrative simply of the extensive use of tax havens by some companies operating in Tanzania, according to information provided in public sources, and is presented to illustrate the difficulties the Tanzanian authorities face in calculating revenue due in Tanzania. Absent a legal framework ensuring easy access to information from tax havens it is almost impossible for national authorities to confidently identify all income taxable in its jurisdiction. Tanzania is no exception.
Box 11: Select examples of the use of tax havens by TNCs operating in Tanzania

Vodacom
Vodacom Tanzania Ltd has a 42 per cent share of the Tanzanian mobile phone subscription market, making it the market leader.\(^78\) It is part of Vodacom Group Ltd, which is 65 per cent owned by Vodafone and based in South Africa where it is listed on the Johannesburg Stock Exchange. Vodacom Group has offshore investment companies in the tax haven of Mauritius; the company’s pre-listing statement for the Johannesburg Stock Exchange detailed two Mauritius subsidiaries. Vodacom International Ltd is referred to in company documents as ‘Vodacom Mauritius’ and holds a majority stake in Vodacom Mozambique and Vodacom DRC. The pre-listing statement also refers to another Mauritius-based subsidiary called Kalum Investments Ltd which has a wholly owned UK subsidiary called Vodacom UK Ltd.\(^79\) Vodacom Group’s latest Annual Report (for the year ended 31 March 2011) also refers to a ‘cash generating-unit’ incorporated in Mauritius called Vodacom Business Africa Ltd.\(^80\)

Tigo
Tigo has a 22 per cent share of the Tanzanian mobile phone subscription market\(^81\) and is the brand name of the international telecommunications company Millicom International Cellular S.A. (MIC). MIC is incorporated in the tax haven of Luxembourg. Its June 2011 Prospectus for the admission to the NASDAQ OMX Stockholm notes that the company’s assets are held ‘mainly but not exclusively through holding companies incorporated in the Netherlands and the Netherlands Antilles,’ (the latter being another tax haven).\(^82\) The same document also shows that the group has a subsidiary in the Cayman Islands (Telemovil Finance Co. Ltd) and a Bermuda incorporated holding company (Amnet Telecommunications Holding Ltd).\(^83\)

Zantel
Zanzibar Telecommunications Ltd (Zantel), another major mobile phone operator in Tanzania, is a subsidiary of the telecommunications company Etisalat, incorporated in the United Arab Emirates. Telecommunications companies pay no corporation tax in the UAE. The group is also reported to have a Mauritius-based incorporated subsidiary.\(^84\)

African Barrick Gold
African Barrick Gold is Tanzania’s largest gold producer and one of the five largest gold producers in Africa. It is listed on the London Stock Exchange and is 73.9 per cent owned by Canada-based Barrick Gold, the world’s largest gold mining company.\(^85\) African Barrick Gold has holdings companies in Mauritius and the Cayman Islands (named BAPL Holdings Ltd and CayCo Tz Ltd respectively) and a ‘Group Finance Company’ incorporated in Barbados (named BarbCo One Ltd). Two of the group’s numerous exploration companies, Barrick Tanzania Holdings Ltd and KMCL Holdings Ltd, are also incorporated in the Cayman Islands.\(^86\)

AngloGold Ashanti
AngloGold Ashanti, which operates the Geita gold mine near Mwanza, had four principal subsidiaries at the time of its May 2009 Prospectus for admission to trading on the London Stock Exchange: one in the US, one in Australia, and two in tax havens: the Isle of Man and Guernsey (called AngloGold Offshore Investments Ltd).\(^87\)
The One Billion Dollar Question: How Can Tanzania Stop Losing So Much Tax Revenue

Tanzanite One
Richland Resources Ltd (formerly TanzaniteOne Ltd) is the world’s largest tanzanite miner. It is listed on the AIM market in London and is incorporated in the tax haven of Bermuda. The company has a Mauritius-based holding company called Afgem International Ltd and a marketing company based in the Caribbean island of Nevis. Its jewellery sales are carried out by subsidiaries in the UK, South Africa and Hong Kong, but it also operates wholly owned subsidiaries involved in Tanzanite sales in Mauritius and the United Arab Emirates.

Resolute Mining Ltd
Resolute Mining Ltd has several subsidiaries registered in Jersey, namely Resolute (CDI Holdings) Ltd, Resolute (Finkolo) Ltd and Resolute (Somisy) Ltd.

Williamson Diamonds Ltd
Petra Diamonds acquired the Williamson diamond mine from De Beers in 2008. The company is incorporated in the tax haven of Bermuda and managed from Jersey where its company registrar is Capita IRG (Offshore) Ltd. Petra Diamonds has a mining and exploration subsidiary registered in the British Virgin Islands called Cullinan Investment Holdings Ltd and two offshore investment holding companies: Petra Diamonds Angola Holdings Ltd, also incorporated in the British Virgin Islands, and Willcroft Company Ltd which is incorporated in Bermuda. The latter holds 75 per cent of the shares in Williamson Diamonds Ltd.

Tanzania Breweries Ltd
Tanzania Breweries Ltd is 33 per cent owned by SAB Miller. According to research by ActionAid, SAB Miller has subsidiaries in the tax havens of Mauritius, the British Virgin Islands, Switzerland, Netherlands Antilles, Nevis, Cyprus, Guernsey, Cayman Islands, Hong Kong, Jersey, Gibraltar, the Isle of Man and Luxembourg. Tanzania Breweries’ capital goods are purchased from a procurement agent called MUBEX, an SAB Miller subsidiary incorporated in Mauritius.
4. Tax evasion and revenue losses

Tax evasion is an illegal practice of avoiding payment of a true tax liability by individuals, organisations or corporations.\textsuperscript{100} The practice is believed to be widespread in Tanzania and involves various activities, although there is – by definition – very little hard information on its extent. In this section, we consider four aspects of this issue.

4.1 Under-reporting of company sales and overstating of losses

A 2008 study for the World Bank noted that tax evasion ‘appears to be a greater problem in Tanzania than in comparator countries’. The study cited managers in Tanzania estimating that a typical firm in their area of activity reported only 69 per cent of its sales for tax purposes (compared to 77 per cent in Uganda and 86 per cent in Kenya). Estimates of the amounts reported for small, medium and large companies ranged from 68 – 83 per cent of sales, with reporting rates highest among larger enterprises. Informal micro-enterprises reported the lowest level of sales – 19 per cent – compared to 28 per cent for formal micro-enterprises.\textsuperscript{101}

The TRA Regional Manager in Mwanza region has said that compliance with tax payments in Mwanza is around 60-70 per cent.\textsuperscript{102} Given that Mwanza is a major business centre in Tanzania with high potential revenues from fish, minerals and cotton farming, tax revenue losses of 30–40 per cent would, in the consideration of the authors, be considerable.

To give one example, the local media has reported that the government is losing more than TShs 65 billion (\$41 million) a year in revenues from tax evasion in the charcoal business.\textsuperscript{103} Mechanisms to collect charcoal taxes are usually poor: Revenue collectors have collection point on the roads through which charcoal traders pass, but these are easily bypassed by traders using alternative roads, for example.

It is clearly not possible to calculate exactly the revenue losses resulting from under-reporting sales and overstating losses. One option, however, is to use the 69 per cent figure cited in the World Bank study above, which is similar to the estimated tax compliance rate in Mwanza. In 2009/10, income, withholding and capital gains taxes paid by companies amounted to around TShs 547 billion (see figures in Table 2 above). If this represented only 69 per cent of the ‘correct’ figure, the loss is around TShs 240 billion (\$151 million) a year.

4.2 Unreported trade

Trade across Tanzania’s borders is believed to be under-reported, and involves smuggling, reducing payments of taxes such as import duties.\textsuperscript{104} A 2008 survey by the East African Business Council found $602 million worth of unrecorded or undervalued cross-border trade transactions at Namanga, on the Tanzania-Kenya border in 2007. The study noted that ‘data from the Kenyan side of Namanga indicates that over $705.67 million worth of exports crossed into Tanzania, yet at the Tanzania side the figures showed that goods received from Kenya within the same period accounted to only $103.18 million’.\textsuperscript{105}

Tanzania has many other borders including those with Uganda (Mutukula), Rwanda (Ngara/Rusumo), Burundi (Ngara), Zambia (Tunduma), Malawi (Songwe-Kasumulu) and Mozambique (Ruvuma). If the observation at the Namanga border is representative of the other borders, then the amount of revenues lost is clearly very substantial. The existence of many unofficial border entry points in the vast land mass of
Tanzania makes its borders highly porous and provides further opportunities for tax evaders. There is also likely to be tax evasion on imports that pass through the various international airports such as the Julius Nyerere International Airport, Kilimanjaro International Airport and Abeid Aman Karume International Airport in Zanzibar and sea ports.

Illegal activities that involve tax evasion are believed to occur in various sectors, including fishing and forestry. The fishing sector employs around 80,000 fishermen and thousands of others engaged in related activities such as processing and trade, and produces an estimated 350,000 metric tonnes of fish, yet it contributes just 1.2-1.4 per cent to GDP, a low figure which some experts put down to tax evasion. As regards forestry, a 2007 report authorised by the Ministry of Natural Resources and Tourism on the logging boom in southern Tanzania, found that rural communities, traders and the government have lost massive potential revenues to wasteful harvesting and processing, non-collection of royalties and under-valuation of forest products. The study found that revenue lost by central and district governments due to the under-collection of royalties reached up to 96 per cent of the potential revenue due. It was estimated that revenue losses for the Forestry and Beekeeping Division amounted to $58 million a year due to under-collection of natural forest product royalties in the districts. Some District Council budgets would have increased several times over if potential timber revenues were actually collected. Substantial revenue losses were also apparent prior to and during timber shipment. For example, the trade statistics showed that China imported ten times more timber products from Tanzania than appear on Tanzania’s own export records. This suggests that Tanzania collected only 10 per cent of the revenue due from these exports.

It is not possible to provide an estimate of tax losses from this form of evasion given lack of other data.

4.3 Alleged financial over-claims in the mining sector

In 2010, the Tanzania Minerals Audit Agency (TMAA) audited 12 mining companies and raised a number of ‘queries’ concerning those companies’ financial claims. It alleged, without specifying which companies, that companies had over-declared their capital allowances and operating expenditures, among other areas – a process which would have reduced their tax liability. Table 9 outlines the key audit queries communicated to the mining companies by the TMAA; these come to a total of $705.8 million. The TMAA noted that these queries received responses from some mining companies, which reviewed and discussed them among their management. However, even after this, there remained a large amount of ‘unresolved queries’, which the TMAA communicated to the TRA for further action. As far as we are aware the companies have not publicly responded to the audit. Table 10 outlines the unresolved queries; worth $251 million.

<table>
<thead>
<tr>
<th>Key audit queries communicated by the TMAA to mining companies for their response, 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wrongly claimed hedge financial liability and losses</td>
</tr>
<tr>
<td>Over-claimed capital allowance</td>
</tr>
<tr>
<td>Unsupported capital and operating expenditure</td>
</tr>
<tr>
<td>Disallowable items</td>
</tr>
<tr>
<td>Wrongly claimed and premature capital deduction</td>
</tr>
<tr>
<td>Understated mineral sales</td>
</tr>
<tr>
<td>Payments for technical services of which withholding tax was not withheld</td>
</tr>
<tr>
<td>Management fees for which withholding tax was not withheld</td>
</tr>
</tbody>
</table>
## Overstated payroll costs
$9.9 million

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Underpayment of Skills Development Levy</td>
<td>$1.7 million</td>
</tr>
<tr>
<td>Unpaid royalties</td>
<td>$0.2 million TShs 466 million</td>
</tr>
<tr>
<td>Unpaid PAYE</td>
<td>TShs 911 million</td>
</tr>
<tr>
<td>Unpaid annual rent for granted mineral rights</td>
<td>0.5 million</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$705.8 million</strong></td>
</tr>
</tbody>
</table>


Table 10: Key Unresolved Audit Queries to Mining Companies Communicated by TMAA to the TRA

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wrongly claimed capital and operating expenditure for tax purposes</td>
<td>$119.2 million</td>
</tr>
<tr>
<td>Wrongly claimed hedge financial liability and losses</td>
<td>$75.3 million</td>
</tr>
<tr>
<td>Disallowable items claimed as allowable expenses</td>
<td>$53.3 million</td>
</tr>
<tr>
<td>Over-claimed wear and tear deductions</td>
<td>$3.3 million</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$251.1 million</strong></td>
</tr>
</tbody>
</table>


If the TMAA’s allegations are true, the figure of $705 million could have resulted in a considerable further tax liability: it is not possible to say how much precisely without calculating the individual companies’ financial position. But a previous gold mining audit (see Box 11) alleged that true tax liability amounted to around a quarter of the figure of alleged over-declared losses: using this guide, $705 million would produce a tax liability of $176 million. Since 2010 was the first year in which the TMAA had conducted audits on the companies, it is possible that similar alleged over-claims could have been made by some companies in previous years. Another estimate is that under-payment of taxes in the mining sector could produce revenue losses of $50–100 million. It is also possible that over-claims are made in other sectors beyond mining.

### Box 12: The 2003 gold mining audit

A 2003 audit of four gold mines commissioned by the government and undertaken by Alex Stewart Assayers alleged that these mining companies were overstating their losses in order to reduce their tax liabilities to the government. Covering 1991-2003, the audit found that the companies had over-declared their losses by $502 million, meaning that, if true, the government would have lost revenues of up to $132.5 million. The audit’s analysis was that one company, AngloGold Ashanti, exaggerated its losses by ‘early charging’ of a tax incentive providing for 15 per cent additional capital allowance on unredeemed capital expenditure and also by ‘improper calculation of the [tax] allowance base by not deducting taxable profit/gain’. According to the audit, another gold mining company, Barrick, over-declared its losses at its Bulyanhulu mine by having ‘erroneously claimed’ the 15 per cent additional capital allowance and, as with AGA’s mine at Geita, by providing ‘unsupported capital expenditure’ for its declared investment and production costs. The audit also stated that Tanzania’s tax losses might be even greater in that ‘6,762 documents are still missing preventing the Auditor from confirming if royalties with an estimated value of $25 million have actually been paid for 939 past shipments’. Despite being widely referred to in the media since 2006, the audit has never been published or formally recognised by the government.
Response by mining companies and the TCME114

In response to a report that included an outline of the findings of the Alex Stewart audit, the Tanzania Chamber of Minerals and Energy (TCME) wrote: ‘We have mentioned many times before and wish to reiterate here that none of the mining companies audited has ever seen an ASA report. It is an essential element of audit procedure that an auditee be given the opportunity to explain any apparent anomalies found during an audit. This has unfortunately never happened and given rise to a lot of speculation on the subject. The report is still a matter of discussion between the government and respective mining companies’.

AngloGold Ashanti stated that it was ‘unbecoming for a respectable company like AngloGold Ashanti to react to unsubstantiated press accusations. The company position was and remains we need to be furnished with the auditing findings or queries to be in a position to react [sic]’. Canadian company Barrick stated: ‘None of the mining companies concerned, including Barrick, have been provided with a copy of the ASA report by either the auditor or the Ministry of Energy and Minerals. It is an essential element of proper audit procedure that an auditee be given the opportunity to explain any alleged anomalies. All the companies concerned have requested copies of the ASA audit report submitted to the government so as to be able to respond accordingly. However, to date, these requests have not been met’.

4.4 The informal sector and revenue loss

Two in five of all Tanzanian households engage in informal sector activities, which account for 40-60 per cent of GDP. A recent TRA report notes that just over half those operating in the informal sector have small-scale wholesale or retail businesses or repair motor vehicles, around a quarter are in service sectors such as education, health and transport and around a fifth are in manufacturing. A full 88 per cent are sole traders and 69 per cent have capital funds below TShs 1.6 million ($1,004).115
The TRA told the researchers for this study that it has no estimate of the full extent of tax evasion in the informal sector. However, a recent TRA report estimates that around 40 per cent of firms in the informal sector do not pay taxes, meaning that ‘TRA is missing over 40 per cent of presumptive income tax revenue’. Thus revenue losses from the failure to collect all taxes from the informal sector can be assumed to be extremely large. Estimates vary:

- The Economic and Social Research Foundation in Tanzania estimates that the revenue lost from not collecting taxes in the informal sector (based on the informal economy accounting for 40 per cent of GDP) amounts to 35-55 per cent of the total tax revenue. This would mean **TShs 1.5 – 2.4 trillion in 2009/10**.

- A study by the Eastern and Southern African Universities Research Programme estimates that tax collections would increase from the current 16 per cent to 20 per cent of GDP if the small-scale informal sector were to pay taxes. Such a 4 per cent increase would bring in extra revenues to the tune of **TShs 1.4 trillion**.

As noted above, most actors in the informal sector are extremely poor and should not be taxed, but others, such as professionals or small manufacturing firms, should be taxed. It is difficult to estimate the size of the informal sector that should be legitimately taxed, but if one quarter is (conservatively) estimated, then this would bring in extra revenues of **TShs 350 – 600 billion a year** ($220 - 377 million) (ie, a quarter of the TShs 1.4 – 2.4 trillion range noted above).
5. The cost to Tanzanians

Tax revenue losses mean less potential money for development. The table below summarises the revenue losses from the different potential sources of tax revenues considered in the previous sections. In total, we estimate that Tanzania is losing revenues ranging from $847 million - $1.29 billion (TShs 1.35 – 2.05 trillion) – thus the median figure is $1.07 billion (TShs 1.7 trillion). This figure is certainly, however, an under-estimate since it does not, for example, include tax revenue losses from other forms of unreported trade such as smuggling, for which no data are available. Neither does it include revenue losses from not fully taxing the informal sector; thus the median figure is slightly lower than the IMF’s estimate tax gap estimate of TShs 1.9 trillion noted in section 1.

Table 11: Summary estimates of tax revenue losses

<table>
<thead>
<tr>
<th>Source of tax revenue losses</th>
<th>Low-end estimates of annual revenue loss</th>
<th>High-end estimates of annual revenue loss</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax exemptions for corporations (certificate holders with Tanzanian Investment Centre, mining sector, other private companies)</td>
<td>TShs 458.6 billion ($288 million)</td>
<td>TShs 458.6 billion ($288 million)</td>
</tr>
<tr>
<td>Illicit capital flows</td>
<td>$28-198 million (TShs 45 – 315 billion)</td>
<td>$300 million (TShs 478 billion)</td>
</tr>
<tr>
<td>Of which Trade mis-pricing</td>
<td>$33-38 million (TShs 53–61 billion)</td>
<td>$150 million (TShs 239 billion)</td>
</tr>
<tr>
<td>Mining sector alleged financial over-claims</td>
<td>$50 -100 million (TShs 80 – 160 billion)</td>
<td>$176 million (TShs 280 billion)</td>
</tr>
<tr>
<td>Company mis-reporting of sales and losses</td>
<td>TShs 240 billion ($151 million)</td>
<td>TShs 240 billion ($151 million)</td>
</tr>
<tr>
<td>Informal sector (Revenue losses from the relatively non-poor who should be taxed)</td>
<td>TShs 350 billion ($220 million)</td>
<td>TShs 600 billion ($377 million)</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$847 million (TShs 1.17 trillion)</strong></td>
<td><strong>$1.29 billion (TShs 2.06 trillion)</strong></td>
</tr>
</tbody>
</table>

The cost of Tanzania’s tax revenue losses is being paid by the poorest people in the country, and the population generally, whose welfare could significantly improve with increased funding to key sectors such as education, health and agriculture. The loss of around $1.07 billion (TShs 1.7 trillion) amounts to over one sixth of the government’s entire expenditure of TShs 9.5 trillion in 2009/10. If the lost tax revenues were spent on education, the budget would double; health spending would more than double and spending on agriculture – a massively under-funded sector – would more than triple. Spending on HIV/AIDS would increase 11-fold, representing a huge injection of funds that could help to eradicate HIV/AIDS from the country. Alternatively, Tanzania could drastically reduce its reliance on foreign aid. The amount lost from taxes is over half the amount in aid received by Tanzania in 2009/10 - TShs 3.2 trillion.122
Table 12: Government budget 2009/10

<table>
<thead>
<tr>
<th>2009/10 Government Budget</th>
<th>Allocation</th>
<th>If tax revenue losses were allocated to this sector, spending would increase by</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total budget</td>
<td>9.5 trillion</td>
<td>over one sixth</td>
</tr>
<tr>
<td>Of which:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Education</td>
<td>1.7 trillion</td>
<td>double</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>1.1 trillion</td>
<td>more than double</td>
</tr>
<tr>
<td>Health</td>
<td>800 billion</td>
<td>more than double</td>
</tr>
<tr>
<td>Agriculture</td>
<td>667 billion</td>
<td>more than triple</td>
</tr>
<tr>
<td>Water</td>
<td>347 billion</td>
<td>nearly six-fold</td>
</tr>
<tr>
<td>HIV/AIDS</td>
<td>163 billion</td>
<td>over 11-fold</td>
</tr>
</tbody>
</table>

Source: Based on figures in MOF, *Budget Digest 2010/11*, June 2010, Table 4
6. Government policy: Positives and negatives

The government is addressing several of the problems outlined in this report. Yet although many policies are positive, the government’s overall approach is insufficient, and is not stemming the huge loss of potential government revenue.

6.1 Increasing revenue collections

In its annual budget speeches, the government has repeatedly stated that it is committed to increasing revenue collections in a number of ways, notably by increasing tax auditing capacity, improving Information Technology (IT) systems and reducing tax exemptions. In one new measure, for example, the Tanzania Communications Regulatory Authority (TCRA) is introducing a national address and postcode database system, which has the potential to increase revenue collections. The current address system makes it difficult to identify and trace all businesses which are potential taxpayers. The TCRA notes that currently the TRA has the capacity to collect TShs 500 billion monthly, but some experts say that amount could be doubled if the physical address system were overhauled.

6.2 Reducing or increasing tax exemptions?

The government recognises that tax exemptions entail a large revenue loss and is taking some steps to reduce them, but progress is slow and the real extent of government commitment is questionable. Finance Minister Mustafa Mkulo said in the 2011/12 budget speech that the government has already taken steps to ‘review procedures for tax exemptions to strengthen control over abuse’ and that government policy was to ‘review and harmonise various tax laws, which have provisions of exemptions, with a view to minimize such exemptions’. Government policy, he said, is to reduce exemptions from their current level of 2.5 per cent of GDP, in his estimate, to ‘at least’ 1 per cent of GDP. This is in recognition of the fact that:

‘The increasing levels of tax exemption contribute to low revenue collection and thus weaken Government ability to finance social economic infrastructure and ultimately reduces the pace of improving well being of our people. Tax exemptions have also created loopholes for tax evasion and revenue leakage’.

Yet only very limited steps have so far been taken. Indeed, the government has recently introduced some new tax exemptions. In the 2011/12 budget speech, delivered in June 2011, the Minister announced that mining and oil/gas companies would be exempt from paying the fuel levy, that VAT special relief would be granted to mining firms that had signed mineral development agreements with the government before July 2009 and that the agriculture sector would receive more VAT exemptions.

Controversially, an income tax exemption was also introduced for allowances paid to employees of government and government-funded institutions.

Both the African Development Bank and the IMF are imploring Tanzania to radically reduce tax exemptions. The ADB notes that:

‘The level of exemptions [has] not only contributed to undermining efficiency and effectiveness of gains resulting from administrative reforms, but also to the substantial revenue loss, probably accounting for most of Tanzania’s tax gap’.

The IMF, meanwhile, says that exemptions are ‘not well monitored’ and that ‘room exists to reduce VAT, import duty and excise tax exemptions and exercise more rigorous control over them’. It has ‘stressed
the importance of broadening the tax base, reducing tax exemptions and strengthening public financial management’. The IMF is specifically calling on the government to:

- Raise the fuel levy and increasing excise tax rates, the latter to the levels in neighbouring Kenya and Uganda
- Reduce VAT exemptions and zero-ratings to broaden the effective tax base
- In mining, to impose withholding taxes on interest paid on foreign currency loans; limit the deductability of debt financing for income taxes; tighten provisions for investment allowances for exploration and development; and ring-fence income tax bases by mines.

Box 12: Benefitting from oil and gas?

There is a danger that Tanzanians will not benefit as much as they could from the newly-discovered oil and gas reserves unless the government improves the way it deals with potential revenues over the way it has dealt with the gold sub-sector.

Petroleum royalties are 12.5 per cent and 5 per cent for onshore projects and offshore projects, respectively, and are collected and administered by the Tanzania Petroleum Development Corporation (TPDC). The production sharing agreements (PSAs) stipulated between the exploration companies and the TPDC also foresee an additional petroleum tax of 25 or 35 per cent, but this has not yet been introduced.

The petroleum tax regime has received much less attention than gold. Companies engaged in exploration activities have been given some tax exemptions on import and export duties and relief on VAT, but these are smaller than provided to gold mining companies. This may change in the future, however. In December 2011, the Finance Minister wrote to the IMF on the subject of taking best advantage of oil and gas revenues and committed the government to drafting a gas and petroleum revenue management bill in order to review the tax regime for the sector and to develop appropriate skills and procedures within the TRA.

There is a clear danger that this will lead to deeper tax concessions in the PSAs.

The oil and gas sub-sector is already been plagued by the same kind of secrecy and lack of transparency evident in the gold mining sector. As the executive director of the Centre for Justice and Democracy, Denis Maringo, has noted, ‘problems affecting oil and gas exploration include secretive contracts, which are signed without the knowledge of communities living in or nearby oil and gas areas or their representatives’. The current PSAs agreed with the TPDC are regarded as ‘complex and corruptive’ by Norwegian People’s Aid, for example. The EITI validation report states that due to incomplete information and poor record keeping, the figures provided by the government on oil, gas and mining revenues are not reliable.

Tanzania is scheduled to comply with the Extractive Industries Transparency Initiative in 2012 or 2013.

Enhancing transparency and developing skills to collect, manage and redistribute the revenues from oil and gas exploitation are thus still major challenges. Another challenge is that the state will start to collect substantial revenues only after the construction phase, which is expected to take several years. ‘Not only will expectations have to be managed during this long transition but there is a risk that policy-makers will mortgage future revenues for immediate consumption’.

6.3 Taxing the informal sector and combating tax evasion

Much more positive are the steps the government is taking to increase taxation of the informal sector. These include the introduction of presumptive taxation in which traders pay a fixed amount of tax per year based on agreement with the TRA. The TRA has also introduced a Block Management System (BMS) that aims to promote compliance by registering all eligible small and medium sized businesses within a particular area
or sector and to gather tax information on the level of economic activities to fight tax evasion. The BMS has simplified the registration of traders and has brought non-payers into the tax net through closer monitoring and collaboration with local government authorities.

The TRA has also taken some measures to plug some tax loopholes and improve the enforcement of legal sanctions against tax fraud. Since 2003, all tax investigations (which were previously settled internally) have been referred to the Legal Services Department. Of 259 investigations made in 2005, 36 cases were referred and of those 32 went to the regional magistrate’s court. However, a recent study by the Christian Michelsen Institute in Norway notes that since magistrates have imposed only fines and not prison sentences, ‘the rewards of tax evasion outweigh the perceived risks. Thus the existing judicial system seems to be a major bottleneck for establishing a credible penalty system for fraud and tax evasion’.

One TRA official has said: ‘It is difficult to say exactly the level of tax evasion but through our sensitisation programmes, more people are now aware about tax evasion and are ready to inform us on the culprits.

Since July 2010, businesses have been required by the TRA to purchase and use TRA’s certified electronic cash registers to book their transactions, which record and remit VAT and tax returns directly to TRA. However, some businesses still avoid paying tax by failing to use these electronic devices.

One reason for tax evasion is the widespread perception that taxes do not contribute to adequate public services. A 2009 survey found that 88 per cent of people surveyed said they would pay more taxes if public services improved. Better use and visible benefits of taxes collected would both encourage some formalization of the informal sector and also widen the tax net.

6.4 Addressing trade mis-pricing?

The government also urgently needs to address the problem of trade mis-pricing. The Income Tax Act 2004 introduced transfer pricing rules, and section 33 requires that any arrangement between associate companies must be conducted at arm’s length (ie, as though trade takes place between two independent parties). Where the Commissioner of the TRA considers that a taxpayer has failed to meet this standard, he has wide powers to make adjustments or re-characterise any amount (see Box 13). The TRA has also stated that it will apply internationally agreed arm’s length principles as set out in the UN and OECD Transfer Pricing Guidelines.

Box 13: Income Tax Act 2004, Section 33 on Transfer Pricing

(1) In any arrangement between persons who are associates, the persons shall quantify, apportion and allocate amounts to be included or deducted in calculating income between the persons as is necessary to reflect the total income or tax payable that would have arisen for them if the arrangement had been conducted at arm’s length.

(2) Where, in the opinion of the Commissioner, a person has failed to comply with the provisions of subsection (1), the Commissioner may make adjustments consistent with subsection (1) and in doing so the Commissioner may –

(a) re-characterise the source and type of any income, loss, amount or payment; or

(b) apportion and allocate expenditure, including that referred to in section 71(2) incurred by one person in conducting a business that benefits an associate in conducting a business to the person and the associate based on the comparative turnovers of the businesses.
However, the government’s transfer pricing rules ‘are largely untested and there is currently a lack of issued guidance’.147 To date the TRA has not issued a Practice Note to clarify what approach it will follow to give effect to these provisions, although it says that transfer pricing guidelines are being drafted.148 There have not yet been any legal cases based on the current legislation and no specific procedures have been laid down by TRA in relation to transfer pricing investigations. The main way the government is addressing transfer pricing is by introducing an International Taxation Unit.149 This is a change in that, until now, there was no dedicated transfer pricing unit within the TRA and queries were handled by the Large Taxpayers Department or Domestic Revenue Department as part of the normal process of reviewing a taxpayer’s income tax affairs.150 It remains to be seen how effective the new unit will be. Given the dynamic and complex nature of business, especially for multinational enterprises operating in Tanzania, it is certainly challenging for the Tanzanian authorities even to identify transfer pricing activities. Moreover, there remains uncertainty about the extent of political will to challenge the activities of companies which the government has long sought to benefit through low taxes and tax incentives.

6.5 Challenges faced by the TRA

The TRA faces a number of further challenges and constraints. Notably, it suffers from corruption: a 2007 analysis by Price Waterhouse Coopers noted that there seemed to be an endemic tax avoidance culture in Tanzania and that some TRA officials seemed to encourage or fall victim to that culture.151 The East African Bribery Index notes that out of 30 Tanzanian institutions, the TRA has the fifth highest prevalence of bribery, with 24 per cent of people surveyed saying they had accessed TRA services upon payment of a bribe.152

The TRA also has a limited audit capacity in specialised sectors such as finance and banking, tourism and telecommunications and suffers from sub-optimal communication and exchange of information between it and other public agencies such as the Ministry of Energy and Minerals.153 Some of these capacity gaps are being addressed by the government and donors, notably by capacity-building support from the Norwegian government and by the Tax Modernisation project, supported by the World Bank, DFID and Danida, which aims to increase revenue collection and improve TRA capacity and expertise.
Policy Recommendations

The government must address tax revenue losses with a sense of urgency and take greater steps to increase revenue collections. Most importantly, it should:

**Tax incentives**

- Undertake a review, to be made public, of all tax incentives with a view to reducing or removing many of them. The aim should be to remove most if not all of the tax incentives granted to the mining sector and to reduce or remove many of those granted in the EPZs. Those tax incentives that are subject to discretionary power by Ministers must be removed. What tax incentives remain should be linked to performance requirements for sectors, such as employment creation and technology transfer.

- Provide annually, during the budget process, a publicly available tax expenditure analysis, showing the cost to the government of the various tax incentives and the beneficiaries. The government should provide details on these in its EITI reports.

- Promote greater coordination in the East African Community to address harmful tax competition, agreeing on minimum rates for certain taxes, to avoid harmful tax competition.

**Mining / extractives sector**

- Make public the findings of audits of individual companies conducted by the TMAA and TRA.

- Review the Mining Act of 2010 to remove the possibility to provide fiscal stabilisation clauses to companies. Renegotiate the terms of all mining agreements with individual companies to bring them into line with Tanzanian legislation and ensure that fair taxes are paid.

- Make all individual mining agreements public by posting them on the Parliament and Ministry of Energy and Minerals websites.

- Review fiscal policy for the oil and gas sector to ensure that tax terms are fair, that agreements are subject to public scrutiny and that Production Sharing Agreements optimally benefit the people of Tanzania.

**Tax Transparency**

- Go beyond the provisions of the voluntary EITI scheme and introduce legislation to compel all foreign companies operating in Tanzania to provide details of their tax payments to the Tanzanian government and make this information publicly available.

- Support international calls that would require transnational corporations to provide details of their tax payments to governments by country (‘country by country reporting’).

- Take steps to increase government and donor support to build the capacity of MPs and civil society to monitor taxation issues in Tanzania.

**Trade mis-pricing/capital flight**

- Make public the TRA’s report on transfer pricing.

- Undertake an analysis, to be made public, of the extent of trade mis-pricing in Tanzania.
• Increase training of officials to recognise transfer pricing and capital flight issues in key sectors, such as mining, and build a stronger capacity to respond to the problem.

• Take steps to ensure implementation of the requirement by companies to provide to the TRA details of their company sales pricing.

• Ensure that the standard ethical procurement principle for associate companies to trade at arm’s length is implemented.

Tax evasion and the informal sector

• Continue to promote messages to potential and actual tax payers and the general public on the negative implications of tax evasion.

• Continue to increase the capacity of the TRA to combat tax evasion and bring parts of the informal sector into tax collections, drawing on donor support.

Responsibility and Accountability

• All companies should be responsible and accountable on all tax issues including transparency to all levels of the government – from village to central government.

• The government should be responsible and accountable to citizens on all issues related to taxes.
Annex: Tax Exemptions in Tanzania

A range of tax exemptions apply to all holders of a Tanzania Investment Centre Certificate of Incentives, which are granted under Section 17 of the Tanzania Investment Act 1997.

Tax incentives for all certificate holders

Investors who meet the minimum investment threshold of $100,000 for local companies and $300,000 for foreign companies are eligible for a Certificate of Incentives issued by the Tanzania Investment Centre. Certificate holders receive:

- Import duty exemption on project capital goods in lead sectors, including agriculture, mining and infrastructure.
- 5 per cent import duty exemption on project capital items in priority sectors, including aviation, commercial buildings, commercial development and microfinance banks, manufacturing, natural resources including fishing, radio and television broadcasting and tourism.
- 100 per cent capital allowance on industrial plant, buildings and machinery and on agricultural expenditure.
- 0 per cent VAT on inputs for mining, agriculture, tourism and goods manufactured for export.
- Under the import duty drawback scheme, businesses are entitled to a refund of duty charged on imported inputs for goods destined for export or to be sold to international institutions like the UN.
- Businesses can carry over losses for five years against future profits.

Tax incentives for investors in Export Processing Zones and Special Economic Zones

Tanzania’s Export Processing Zones Act was passed in 2002 and sought to attract FDI and promote exports, increase employment opportunities and promote technology transfer. The Act requires that at least 80 per cent of the goods produced or processed in an EPZ should be for export. The annual turnover of companies should not be less than US$ 500,000 for foreign investors and US$ 100,000 for local investors. In 2006, the government established Special Economic Zones (SEZs), which include EPZs, Free Ports, Free Trade Zones, Industrial Parks, Science and Technology Parks, Agricultural Free Zones, and Tourism Development Zones. Investors qualify under the SEZ scheme if they demonstrate that their investment is new, achieve a minimum annual export turnover of $5 million for foreign investors and $1 million for domestic investors, provide adequate environmental protection and utilize modern production process and new machinery. The tax incentives in EPZs and SEZs include:

- Exemption from corporate income tax for the first 10 years.
- Exemption from withholding tax on rent, dividends and interest for the first 10 years.
- Import duty exemptions on raw materials and capital goods imported for manufacturing goods in the EPZs.
- Exemptions from VAT charges on utilities and wharfage.
- Exemptions from all taxes and levies imposed by Local Government authorities for the first 10 years.
- Unlimited repatriation of profits.
Tax incentives for ‘strategic investors’

Tanzania’s ‘Strategic Investor Status’ accords various tax incentives to companies investing more than $20 million. The Tanzania Investment Centre states: ‘For a big project of over $20 million offering specific/great impact to the society or economy, investors can request for special incentives from the Government.’ Thus some companies, notably foreign mining and agribusiness companies, have an individual fiscal agreement with the government, some of which offer special concessions to individual companies but which have never formally been made public.

Tax exemptions for mining companies

Mining companies are given various tax incentives and exemptions, including in individual Mining Development Agreements the government has signed with them. Although a new Mining Act was introduced in 2010 – replacing the Mining Act of 1998 – the mining agreements signed before 2010 remain in force. Their terms often vary, but many contain, and others are believed (they have not formally been made public) to contain, fiscal ‘stabilisation’ clauses. This means that the range of tax incentives provided in the individual agreements are still likely to apply even under the new Act. The tax exemptions enjoyed by mining companies include:

- zero import duty on fuel (compared to the standard current levy of TShs 200 per litre) and on imports of mining-related equipment during prospecting and up to the end of the first year of production; after this, they pay 5 per cent.
- exemption from capital gains tax (unlike other companies in Tanzania).
- special VAT relief, which includes exemption from VAT on imports and local supplies of goods and services to mining companies and their subcontractors.
- The ability to offset against taxable income the cost of all capital equipment (such as machinery or property) incurred in a mining operation. Non-mining companies are entitled to a 100 per cent depreciation allowance only for the first five years of operations.
- A reduced rate of stamp duty, at 0.3 per cent. This is included in several mining agreements signed between the government and the mining companies, even though the rate of stamp duty is set by law at 4 per cent.
- A maximum payment of local government taxes up to $200,000 a year, which is lower than the 0.3 per cent of turnover required by law.

Tax incentives for agricultural investors

Agricultural investors are offered:

- Zero-rated import duty on capital goods and all farm inputs
- Import duty drawback on raw materials for inputs used for exports
- Deferment of VAT payment on project capital goods
- Zero-rated VAT on agricultural exports and for domestically produced agricultural inputs

Further tax exemptions are provided under the government’s ‘Kilimo Kwanza’ initiative, which aims to promote commercialisation and new technology in farming.
• VAT is exempt on a number of items such as fuel used for the transportation of agricultural products like sugar cane, sisal and tea from the farm to the processing factory, animal feed and agricultural machines such as combine harvesters.

• Import duty is exempted on tractors.

**Other tax exemptions**

Newly-listed companies on the Dar Es Salaam Stock Exchange with at least 30 per cent of their shares issued to the public pay only 25 per cent **corporate income tax** (compared to the standard 30 per cent) for the first three years.\(^{164}\)

Shares of companies listed on the Dar Es Salaam Stock Exchange are exempt from paying **capital gains tax** (which normal rate is 30 per cent).\(^{165}\)

There are number of items exempt from **VAT**, in addition to those mentioned above, such as insurance, education, financial services and tourist services. Goods provided under technical aid or donor-funded projects and voluntary organisations are relieved from **VAT**.\(^{166}\)

**Tax incentives for investors in Zanzibar**\(^{167}\)

Zanzibar has established Free Economic Zones and Free Ports and also offers investors various incentives, the most important of which include:

• Exemption from corporate income tax (in an EPZ: 100 per cent for the first 10 years then 75 per cent for the next 10; in a Freeport: 100 per cent for the first 20 years).

• Exemption from import duty on machinery, equipment, construction/raw materials.

• Exemption from taxes on goods for export.

• Exemption from taxes on dividends for the first 10 years (in an EPZ only).

• Exemption from all local taxes for goods produced in the zone.
References

10. The size of the informal economy is by definition hard to estimate. The government and the Economic and Social Research Foundation estimate 40 per cent (TRA, Review of Informal Sector for Taxation Purposes, Draft, January 2011, p.xii; ‘Informal Sector Taxation in Tanzania’, TAKNET Policy Brief, No.12, 2010, p.1); A recent World Bank analysis suggests around 60 per cent (Friedrich Schneider et al, Shadow Economies all over the World: New Estimates for 162 Countries for 1999 to 2007, World Bank, June 2010); the Tax Justice Network has recently used a figure of 56.3 per cent (The Cost of Tax Abuse: A Briefing Paper on the Cost of Tax Evasion Worldwide, November 2011)
11. ‘TRA has no tax evasion statistics’, Daily News, 11 August 2010
13. ‘Tax compliance is a legal obligation’, Daily News, 12 December 2011, citing a recent TRA report
14. World Bank, Tax Modernisation Project: Implementation Status and Results, November 2011, p.3
17. African Development Bank, Domestic Resource Mobilisation for Poverty Reduction in East Africa: Tanzania Case Study, November 2010, p.34
19. IMF, First Review under the Three-Year Arrangement under the Extended Credit Facility, 15 June 2011, p.20
22. This IMF analysis does not define what it means as the ‘tax gap’. We understand it refers to uncollected revenues from the informal sector and also from tax exemptions. The ‘tax gap’ is usually referred as ‘the difference between what is legally due under the law, and what the government will be able to collect’ (IMF Task Force on Harmonization of Public Sector Accounting—Working Group 2, July, 2004, http://www.imf.org/external/np/sta/tfhsa/2004/trjd.pdf
23. IMF, Staff Report for the 2011 Article IV Consultation and Second Review under the Policy Support Instrument, 21 April 2011, p.25; Tax gap in TShs is based on GDP figures of TShs 30,321 billion in 2009/10


To obtain a certificate of investment, local companies must invest a minimum of $100,000 and foreign companies $300,000. ‘Corporate Tanzania: Business, Trade and Investment Guide 2010/2011’, p.57, www.corporate-tanzania.com

Analysis by the Non Governmental Organization (NGO), Uwazi, based on figures from the TRA, shows that losses from incentives and exemptions amounted to an average of TShs 775 billion a year in the four years 2006/07 – 2009/10. These amount to 2.3 – 4.3 per cent of GDP. Uwazi, ‘Tanzania’s Tax Exemptions: Are they too high and making us too dependent on Foreign Aid?’, *Policy Brief*, TZ.12/2010E, p.3. The East African Community secretariat – covering exemptions on import duties alone - estimates that revenue losses from tax exemptions amounted to US$ 435.9 million in 2008 and an average of US$ 370 million (TShs 811 billion) in the three years 2006-08. (*The EAC Trade Report, 2009, http://www.eac.int/statistics/index.php?option*).


*African Development Bank, Domestic Resource Mobilisation for Poverty Reduction in East Africa: Tanzania Case Study*, November 2010, p.20


An average of 2.9 per cent in for 2008-2010 as calculated in Uwazi, ‘Tanzania’s Tax Exemptions: Are they too high and making us too dependent on Foreign Aid?’, *Policy Brief*, TZ.12/2010E, p.7. The government stated that tax exemptions amounted to 2.5 per cent of GDP in 2010/11 (Finance Minister, Budget Speech 2011/12, p.25).

‘List of best taxpayers ignites debate’, *The Citizen*, 29 August 2011


TMAA, *Annual Report 2010*, pp.9, 19

IMF, *Staff Report for the 2011 Article IV Consultation and Second Review under the Policy Support Instrument*, 21 April 2011, p.17


How Can Tanzania Stop Losing So Much Tax Revenue

Policy Forum, ‘How Much Revenue Are We Losing?’, Policy Brief, March 2009


‘Documents confirm Tanzania is looking at mining “super profit tax”’, Reuters, 8 June 2011; ‘AngloGold says any Tanzanian “super profits” tax will not apply’, Reuters, 8 June 2011


IMF, Kenya, Uganda and United Republic of Tanzania: Selected Issues, 1 December 2006, p.10


Global Tax Simplification Team of the IFC Investment Climate Advisory (April, 2011), presentation at the EAC’s Validation Workshop of the Study of Double Taxation Avoidance Model and the Code of Conduct Against Harmful Tax Competition held in Arusha, April 2011. There are many other problems with tax incentives. The application of different rules complicates tax administration and increases costs while there are social costs caused by corruption and rent-seeking where the administration of tax incentives is abused, as is often the case. Tax incentives are also prone to abuse when the incentive is exhausted and the promoters of the business fraudulently wind it down and simultaneously establish another entity to be accorded the same incentives. Tax incentives also tend to favour elite private investors who actually have adequate own capital. Once incentives are provided, they are politically difficult to remove. In some cases, incentives are a further waste of resources in that many companies would anyway invest without the incentive. H.Zee et al, ‘Tax Incentives for Business Investment: A Primer for Policy Makers in Developing Countries’, World Development, Vol. 30, No. 9, 2002, pp. 1497-1516

IMF, Kenya, Uganda and United Republic of Tanzania: Selected Issues, 1 December 2006, p.11

At a Trade Justice Network -Africa/ActionAid roundtable in Nairobi in July 2011, John Njiraini, the Commissioner of Domestic Taxes in Kenya, confirmed this truism. He cited the example of a large tax payer, a blue chip company in Kenya which increased the level of investment considerably within months of KRA’s withdrawal of some previously enjoyed incentive. Apparently, certain categories of taxpayers, mostly, large, were allowed to offset VAT refunds against other tax liabilities, a facility which was withdrawn due to challenges in management.


‘The “industrialised nation” dream must come true’, Tanzania Daily News, 17 April 2012

Charles Domician, An Evaluation of Tanzania’s EPZ Programme – Challenges and Prospects, 2009, p.28

Charles Domician, An Evaluation of Tanzania’s EPZ Programme – Challenges and Prospects, 2009, p.30

The size of the informal economy is by definition hard to estimate. The government and the Economic and Social Research Foundation estimate 40 per cent (TRA, Review of Informal Sector for Taxation Purposes, Draft, January 2011, p.xii; ‘Informal Sector Taxation in Tanzania’, TAKNET Policy Brief, No.12, 2010, p.1); A recent World Bank analysis suggests around 60 per cent (Friedrich Schneider et al., Shadow Economies all over the World: New Estimates for 162 Countries for 1999 to 2007, World Bank, June 2010); the Tax Justice Network has recently used a figure of 56.3 per cent (The Cost of Tax Abuse: A Briefing Paper on the Cost of Tax Evasion Worldwide, November 2011)

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Harry Kitiliya, ‘Tax Administration Reforms in Tanzania – Experience and Challenges’, April 2011, section 2.2


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IMF, First Review under the Three-Year Arrangement under the Extended Credit Facility, 15 June 2011, p.20

Nehemiah Osoro, Domestic Resource Mobilisation in Sub-Saharan Africa: The Case of Tanzania, 2010

IMF, Seventh Review under the Policy Support Instrument, 18 May 2010, p.20

This IMF analysis does not define what it means as the ‘tax gap’. We understand it refers to uncollected revenues from the informal sector and also from tax exemptions. The ‘tax gap’ is usually referred as ‘the difference between what is legally due under the law, and what the government will be able to collect’ (IMF Task Force on Harmonization of Public Sector Accounting—Working Group 2, July, 2004, http://www.imf.org/external/np/sta/tfhsa/2004/trjd.pdf

IMF, Staff Report for the 2011 Article IV Consultation and Second Review under the Policy Support Instrument, 21 April 2011, p.25; Tax gap in TShs is based on GDP figures of TShs 30,321 billion in 2009/10
THE ONE BILLION DOLLAR QUESTION: How Can Tanzania Stop Losing So Much Tax Revenue


102 Dassu Stephen, ‘Mwanza TRA exceeds target by over 100 per cent’, Daily News, 2 December 2011

103 ‘Out of the estimated 36 million bags of charcoal consumed in the country annually, official records show that hardly 6bn out of 72bn estimated revenue generated from the local trade annually lands into the government account...No doubt the estimated 66bn/- revenue collected ended in individual pockets because charcoal arrived at the market in urban centres, it has to go through several checkpoints to verify payment of revenue.’ ‘Treasury loses 65bn/- revenue from charcoal’, Daily News, 9 December 2010


106 Masato Masato, ‘TRA now eyes forestry, fishery for revenues’, Daily News, 23 February 2011. The report notes that ‘the negligible contribution of the forestry and fishery subsectors to the national economy has prompted a risk assessment study by the Tanzania Revenue Authority (TRA) to boost tax revenues from the sub-sectors’.

107 Simon Milledge et al, Forestry, Governance and National Development: Lessons Learned from a Logging Boom in Southern Tanzania, 2003, p.3


109 Interview with expert in Dar Es Salaam, March 2012.


111 Alex Stewart Assayers report, ‘The evaluation of the gold auditing programme’, mimeo, p.6

112 Alex Stewart Assayers report, ‘The evaluation of the gold auditing programme’, mimeo, p.7

113 Alex Stewart Assayers report, ‘The evaluation of the gold auditing programme’, mimeo, p.10

114 See Mark Curtis and Tundu Lissu, A Golden Opportunity: How Tanzania is Failing to Benefit from Gold Mining, October 2008, p.26


116 TRA response to questions by the researchers, 27 February 2012

117 TRA, Review of Informal Sector for Taxation Purposes, Draft, January 2011, pp.xvii, 92; The Comptroller General has estimated that around 56 per cent of people in the informal sector do not pay taxes: Aisia Rweyemamu, ‘56 pc in informal sector don’t pay taxes – CAC’, The African on Saturday, 3 March 2012


121 Based on GDP figures of TShs 34,750 billion in IMF, Staff Report for the 2011 Article IV Consultation and Second Review under the Policy Support Instrument, 21 April 2011, p.24. Another estimate is from the Tax Justice Network, which estimates that the failure to tax the informal sector costs Tanzania $1.92 billion (TShs 2.8 trillion at the then exchange rate) a year. This is based on the shadow economy amounting to 56.4 per cent of GDP. It also appears to assume that currently no taxes are being paid in the informal sector at all although as noted above, this is disputed by the Tanzanian authorities. Tax Justice Network, The Cost of Tax Abuse: A Briefing Paper on the Cost of Tax Evasion Worldwide, November 2011


123 Finance Minister, Budget Speech 2011/2012, pp.25-6, www.mof.gov.tz
In June 2011, for example, it was reported that the government was considering levying a ‘super profits tax’ on windfall earnings from mining. But AngloGold Ashanti, which operates the country’s largest gold mine, stated that the introduction of such a tax would not affect its tax payments since its mining agreement with the government has a fiscal stabilisation clause, forbidding the government from raising taxes on the company.

‘Documents confirm Tanzania is looking at mining “super profit tax”’, Reuters, 8 June 2011; ‘AngloGold says any Tanzanian “super profits” tax will not apply’, Reuters, 8 June 2011

See Mark Curtis and Tundu Lissu, *A Golden Opportunity: How Tanzania is Failing to Benefit from Gold Mining*, October 2008, for discussion of fiscal incentives provided to mining companies and for the full sources in the section that follows

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Ministry of Finance, ‘Macroeconomic Policy Framework for the Medium Term Plan Budget’, www.mof.go.ke. In the 2011/12 budget, the Minister of Finance stated that Kilimo Kwanza is expected to create employment, particularly for the rural youth, and that the World Bank plans to finance this initiative with US$ 60 million, the equivalent of Tshs 92.8 billion; http://www.mof.go.tz. These exemptions are likely to benefit mainly large-scale, commercial farmers and bypass the majority of Tanzanians who are small-scale, subsistence farmers. The VAT exemptions on fuel, for example, apply only to organised farmer groups not individual smallholders while the import duty exemptions on tractors are largely irrelevant to smallholders unable to afford such equipment which anyway is not relevant to working small plots of land. Policy Forum, ‘Do Kilimo Kwanza Exemptions Benefit Poor Farmers?’, *Policy Brief 3:10*, 2010


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